TO CONSIDER S. 2446, AND OTHER SMALL BUSINESS PROCUREMENT REFORMS

HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

SECOND SESSION

TO

CONSIDER S. 2446, AND OTHER SMALL BUSINESS PROCUREMENT REFORMS

SEPTEMBER 16, 1982

Printed for the use of the Committee on Small Business

U.S. GOVERNMENT PRINTING OFFICE
99-736 O
WASHINGTON : 1982

S721-18

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September 16, 1982:
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TO CONSIDER S. 2446, AND OTHER SMALL BUSINESS PROCUREMENT REFORMS

THURSDAY, SEPTEMBER 16, 1982

U.S. SENATE,
COMMITTEE ON SMALL BUSINESS,
Washington, D.C.

The committee met, pursuant to notice, at 9:30 a.m., in room 424, Russell Senate Office Building, Hon. S. I. Hayakawa (acting chairman of the committee) presiding.

Present: Senators Hayakawa and Dixon.

Also present: Robert J. Dotchin, staff director; Kimberly A. Elliott, professional staff member; Alan L. Chvotkin, minority chief counsel; and Dorothy Olsen, hearing clerk.

STATEMENT OF HON. S. I. HAYAKAWA, A U.S. SENATOR FROM THE STATE OF CALIFORNIA

Senator HAYAKAWA [acting chairman]. Good morning.

The Senate Committee on Small Business has convened this morning to consider S. 2446, the Small Business Procurement Reform Act of 1982 and other small business procurement reforms. I am delighted that Senator Specter will be joining us this morning to present testimony in support of his legislation.

I believe it is timely for the committee to consider small business procurement reform legislation and to identify possible solutions to common impediments to small business participation in the Federal procurement system. I say timely because recent Governmentwide procurement statistics show that small business participation on Federal contracts is declining from its already low base of 23.6 percent, while Government procurement spending is increasing.

As a matter of fact, Federal agencies will spend more than $120 billion on direct procurement during fiscal year 1982—a new record despite the Government's attempt to curb spending.

In my opinion, if procurement spending is on the rise, then small business participation on public contracts should be increasing, too. I hope that this hearing will help shed some light on why this is not the case and what the administration and the Congress can do to remedy this situation.

The legislation before us today does address several aspects of the Federal procurement process that currently present obstacles to small business participation in the system. The committee will focus its attention on two major components of the legislation: Section 5, relating to component bidding on large system procurements, and section 6, concerning contract arbitration panels.

This committee has already acted favorably on legislation similar to the bill's provisions on minimum time periods for advertising in the Commerce Business Daily. In fact, following the two hearings I chaired on problems encountered by small businessowners who tried to use the CBD, the committee marked up, and the Senate passed, S. 1947. I am still very hopeful that the legislation, that would establish minimum criteria for advertising in the CBD, will become law before the end of the 97th Congress.

Although we will concentrate on the major provisions of S. 2446 this morning, the committee has invited the witnesses to identify additional procurement reforms that might benefit the small business community. For example, the General Accounting Office will testify on its recent report in the SBA' spare parts breakout program, a program that could offer unlimited procurement opportunities for small firms if it was implemented aggressively by the Defense Department.

I know that several of our other witnesses will present their views on additional procurement reforms. I am especially eager to hear from Mr. Donald Sowle, Administrator of the Office of Federal Procurement Policy, on how the administration's omnibus procurement proposal is progressing and how it might benefit small firms.

In summary, I believe that, as the world's largest single purchaser of goods and services, the U.S. Government has an obligation to guarantee small busineses their fair share of the Federal procurement dollar. Developing the capacity of small firms to do business with the Government is essential to the economic well-being of the country and to its national security. We must not allow small business participation to decline further or this country's ability to mobilize its defense industrial base will then continue to deteriorate.

In the interest of time, I would like to ask each of our witnesses to limit his or her oral testimony to 5 minutes. This will allow me and other members of the committee more time to question each of you. Your written statements will be included in the hearing record in their entirety.

Because of a sudden change in his schedule, Senator Specter will not be able to lead off the hearing this morning. However, he will be joining us a little later in the day.

At this time I would like to insert into the hearing record a statement of Senator Weicker, chairman of this committee, and Senator Nunn, ranking member.

[The prepared statements of Senators Weicker and Nunn follow:]

STATEMENT OF HON. LOWELL WEICKER, JR., A U.S. SENATOR FROM THE STATE OF CONNECTICUT

The Committee on Small Business is meeting today to consider the issue of small business procurement reform. We want to know why it is that small firms receive less than one quarter of the one hundred plus billion dollars the Federal Government spends every year on direct Federal procurement; why small firms are reluctant to enter this vast Federal marketplace; and what this committee and the United States Congress can do to make Federal contracting more attractive for this Nation's small businesses.

Throughout the 97th Congress, Federal procurement policies have been a major concern of the Small Business Committee. Members of this committee joined me in battling the late payments problem faced by many Government contractors, a battle that culminated in enactment of the Prompt Payments Act. This new law forces the

Government to follow a standard business practice: Either pay your bills on time or pay interest to your contractors.

This committee also took the lead in creating increased research and development opportunities for small business through it promotion of S. 881, the Small Business Innovation and Development Act. Enacted in June of this year, this law creates a special small business innovation program that will help guarantee that small firms get a fairer share of the Federal R&D dollar.

Finally, the committee took quick action when it learned that small businesses were not receiving adequate or timely notice of upcoming Federal contracting opportunities. The committee reported out S. 1947, a bill to establish minimum time periods for advertising in the Commerce Business Daily (CBD). The bill passed the Senate in May, and I am extremely hopeful that the Congress will enact this important small business procurement reform legislation before the 97th Congress adjourns.

Yet, despite all of these actions, I believe that we have only begun to scratch the surface of what can be done in the procurement area to help small firms. The bill we are presented with today contains some good concepts which I believe can provide the basis for legislation that will bring us one step closer to an equitable procurement system. For example, I think that the whole "breakout" issue—both component breakout of large systems and spare parts breakout—is a fruitful area for small business participation, provided such programs are implemented to their full potential by Federal procuring agencies. Along those lines, let me just say that I was delighted to learn that the Department of Defense recently extended the comment period on its proposed "high dollar spare parts breakout program" regulations. I believe that this action will give more small firms an opportunity to offer their views on this important, yet, complex issue. I can only hope that the final regulations will exhibit an equally thoughtful response by the Defense Department.

And, I hope that this hearing brings ideas for other small business procurement reforms to light. Our witnesses from the small business community—men and women involved in Federal contracting on a day to day basis—are sure to have excellent suggestions that have not yet been considered by the Congress. I hope administration witnesses will listen carefully to these small business representatives and take their suggestions into account during the formation of all omnibus or small business procurement reform policy.

I wish to extend my deep appreciation to Senator Hayakawa for chairing the hearing this morning. He has been a consistent leader in the procurement field on this committee. His dedication to providing increased procurement opportunities to small firms has been demonstrated by his willingness to sponsor three Federal procurement seminars. In addition, he has chaired three hearings on the issue of Government competition with the private sector, as well as two hearings on the Commerce Business Daily.

Finally, I would like to thank each of the witnesses for joining us today to share their views on procurement issues with the committee.

STATEMENT OF HON. SAM NUNN, A U.S. SENATOR FROM THE STATE OF GEORGIA

Mr. Chairman, today the Senate Small Business Committee continues its hearings on the Federal procurement process, and ways in which we can further open up the Federal procurement process for small businesses. The Federal Government is among the largest purchasers of goods and services in the United States, with procurements totalling over $110 billion annually. According to the Office of Federal Procurement Policy, almost one-fifth of the Federal budget was committed through over 17 million "contract actions".

It is not surprising, therefore, that there is so much interest in the policies, procedures, and purchases made by the Federal government. It is also not surprising that small businesses are becoming more active and aggressive in seeking prime and subcontracts from Federal agencies. I am pleased to note that we in the Senate Small Business Committee have taken seriously our responsibilities to fulfill the mandate which was enacted in the Small Business Act that:

"It is the declared policy of the Congress that the Government should, aid, counsel, assist, and protect, insofar as possible, the interest of small business concerns in order . . . to insure a fair proportion of the total purchases and contracts or subcontracts . . . be placed with small business enterprises." [1]

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[1] Sec. 2(a) of the Small Business Act, as amended.

The activism of this Committee on behalf of small business is enviable. Most notably, I believe, were the amendments which the Senate Small Business Committee, and the Senate Governmental Affairs Committee undertook in the 95th Congress—amendments to the Federal procurement process which ultimately were signed into law as Public Law 95-507. In my view, that statute put small business up front in the procurement planning, and utilization, in the Federal procurement system. As my colleagues know, that law, among other things:

(1) Establishes an Office of Small and Disadvantaged Business Utilization reporting to the head of each procuring agency, and charged with the responsibility for implementing the procurement provisions of the Small Business Act and other laws within each agency;

(2) Requires a formalized "goal-setting" between the Small Business Administration and the procurement agencies, for targeting participation by small and disadvantaged firms in procurement actions in excess of $10,000;

(3) Sets aside exclusively for small business each contract for the procurement of goods and services which has an anticipated value of less than $10,000 and which is subject to small purchase procurement procedures; and

(4) Imposes a requirement that Federal prime contracts in excess of $500,000 ($1 million for construction) have mandatory subcontracting clauses, and a plan for the increased utilization of small business as subcontractors.

Each of these requirements separately, and the procurement scheme in its totality, was designed to open up the procurement process for greater opportunities for small business.

In this Congress, we have enacted the Prompt Payment Act which is designed to insure that the Federal government pays its bills on time, or, like the private sector, pays interest on its overdue accounts.

In addition, through a variety of amendments to the Armed Services procurement Act, during the past several years, Congress has begun an effort to simplify Defense procurements. Undersecretary of Defense Carlucci announced a 31 point procurement initiative program to further streamline the internal DOD program and efforts are underway to implement those changes. One of the key elements of those "Carlucci initiatives" is the requirement for increased competition and utilization by small business in Defense contractors. Depending on the choice of sources for the numbers, it has been reported that the Defense Department procurement is between 45 and 69 percent competitive.

We have also enacted the Small Business Innovation Development Act to increase the direct small business participation in Federal agency research and development activities. This committee has taken the lead to develop, and report, amendments to the Commerce Business Daily (S. 1947). This proposal is designed to increase the effectiveness of that document as a source of timely and quality information on the Federal Government's procurement intentions, with the hope that improved notice and information will result in increased competition for that good or service. Certainly increased small business knowledge, and opportunities, can lead to increased bidding and winning, but the bill is not limited to small business alone. I am pleased that the Senate has already passed this important legislation, and I am hopeful that we can find a way to get this proposal to the President in this session of Congress.

Senator Weicker and I have also sponsored legislation (S. 1782) which would eliminate the current practice in some Federal agencies of "retaining" a certain portion of a construction contractor's progress payments. Here too, the procurement process is having an impact on the ability of many smaller enterprises to remain in business, without any apparent need for the requirement by the Federal Government. This proposal has already had hearings in the Senate Governmental Affairs Committee, on which I also serve, and could be reported to the full Senate in the very near future.

Earlier this year, the Office of Federal Procurement Policy, pursuant to statutory mandate, sent to the Congress their proposal for a uniform Federal procurement policy, including proposals to "conform" the two major Federal statutes dealing with procurement. A project to combine the Federal acquisition regulations is also nearing completion. Each of these efforts serves to highlight the importance of the Federal procurement process to the Government as it seeks to buy goods and services in the most efficient manner and at the lowest price, to the contractors who seek maximum opportunities to compete for the Federal contract dollar, and for the American people who are the ultimate beneficiaries of much of the Federal procurement effort.

Each time members and committees of Congress review the complicated Federal procurement process, either is case work on behalf of our constituents, or in the form of legislation, we find ways we can improve on the process. I believe Senator Specter's proposal (S. 2446) which we are considering today adds an important element to that continuing debate. I was pleased to be an original cosponsor of this proposal because it serves as an excellent focal point for the small business community and the Congress to review several critical elements of the procurement process.

One of the policy statements which the legislation proposes to include in the Small Business Act is the requirement that all Federal agencies must review their major systems acquisitions for opportunities to subdivide the procurement action so as to maximize small business participation. This is often referred to as "component breakout". In addition, another form of "breakout" for increased competition by small business is in the field of follow-on spare parts to original equipment purchases. Today, we will hear from the Small Business Administration about their targeted program of assigning SBA field representatives in selected Air Force procurement installations with the specific mission of increasing the breakout of spare parts. I am pleased to note that in my own state of Georgia, Robins Air Logistics Center has been actively involved in the pilot program, with impressive results in both savings to the Federal government and performance by the small business community. The General Accounting Office will also provide us with testimony on their review of this pilot effort.

The Department of Defense has had a "High Dollar Spare Parts Breakout Program" since 1969. DOD has proposed to integrate that program into the Defense Acquisition Regulations. Some contractors and others have expressed concern about the implemention of that policy, and I for one would welcome comments on the success and problems with the DOD program.

Mr. Chairman, as we focus on the success that we have seen demonstrated in the breakout programs (either in spare parts or components), and continue to encourage agencies to adopt this approach, there are several instances that I am aware of where agencies have taken conscience action to consolidate, or "bundle" potential individual procurement opportunities into a single solicitation. In one instance, in particular, the Army has decided to solicit bids to upgrade its base telephone systems for all installations in the continental United States, Alaska, Hawaii, and Korea. Although this "requirement" has been subdivided into four separate contracts, it is the geographical areas that the Army expects to be serviced by these contracts that has created a virtual barrier to realistic competition, and appears to virtually foreclose any small business competition. I have already asked the General Accounting Office to review the background, and more importantly, assess any justification for the Army's consolidation in this important area. This contracting approach vividly displays why we must be careful to insure that the procurement process does not create artificial barriers to full and fair competition.

There are other innovative procurement proposals dealing with arbitration and increasing small business involvement in the acquisition process in Senator Specter's bill that we will hear about today. Each of these concepts is valuable in stimulating further discussions within this Committee, the Congress, and the procurement community and I would hope that we would follow up on them with future hearings.

Mr. Chairman, for many businesses, large and small, Federal purchases are their primary business. In growing numbers, contractors are turning to the Federal system as a means of augmenting slumping private sector purchases. But regardless of the reasons, we have a responsibility to the taxpayer, to the small business sector, and in some cases to the security of this Nation, to insure that we are able to provide the quality goods and services that agencies require in a timely manner, at a fair price. I look forward to the testimony today, and to the continued activities by this Committee on behalf of the small business contractor.

Senator **Hayakawa**. I would like to announce one change in the panel of small business contractors. Mr. Bruce Hahn, manager of the Government Relations Division of the National Tooling and Machinery Association will be substituting for Mr. McCullough.

Senator Dixon, do you have any opening remarks?

STATEMENT OF HON. ALAN J. DIXON, A U.S. SENATOR FROM THE STATE OF ILLINOIS

Senator **Dixon**. Thank you, Mr. Chairman.

I join with Senator Specter, yourself, and others in cosponsoring the Small Business Procurement Reform Act of 1982. In the past 2 years I have sponsored or cosponsored two Federal procurement conferences in Illinois. These conferences attracted approximately 1,500 businessmen and businesswomen from throughout my State. S. 2446 addresses some of the problems business people brought forth at our Illinois conferences.

Mr. Chairman, every year the Federal Government spends more than $100 billion to buy a vast variety of services and supplies from businesses in the private sector. These purchasing dollars create real economic growth opportunities. However, Mr. Chairman, many firms shy away from a chance to make the Federal Government one of their customers. Some firms lack the information necessary to participate in the system. Others have legitimate fears about the amount of paperwork involved. This legislation will address some of these obstacles.

We need more firms throughout this great country of ours bidding on a competitive basis. More competition will mean savings to the taxpayers.

Senate bill 2446, Mr. Chairman, will help strengthen our country's industrial base. When the number of firms and the number of people providing goods for the military is increased, our country's ability to mobilize behind any increased need for equipment is vastly improved.

Mr. Chairman, I congratulate Senator Specter, yourself, and the other cosponsors of this bill. I look forward to the day in this Chamber when I can vote for final passage of this bill to help small business men and women throughout the United States.

I will have the privilege in a moment on this first panel, Mr. Chairman, of introducing a personal friend, Mr. Leo Dondanville of Springfield, Ill.

I thank the Chair.

Senator HAYAKAWA. I would like first to call upon Dr. Earl Hess, president of Lancaster Laboratories, Inc., of Lancaster, Pa. Dr. Hess testified last year before this committee. I look forward with pleasure to hearing from him again.

Then we will have Mr. Bruce Hahn, representing the National Tooling and Machinery Association; Mr. Leo Dondanville, Hanson Engineers, Inc., Springfield, Ill.——

Senator DIXON. Mr. Chairman, may I briefly have the privilege of introducing a personal friend, Mr. Dondanville, of Springfield, Ill.

Senator HAYAKAWA. Yes, indeed.

Senator DIXON. He is a friend of 20 years and an engineer in my State of Illinois with a distinguished record in public as well as private service. Leo is a spokesman for consulting engineers on the statewide level and has directed engineering projects in most States in the Union.

Mr. Chairman, we are pleased and fortunate, indeed, to have a man such as Leo Dondanville with us today.

Senator HAYAKAWA. Thank you, Senator Dixon.

Now let's hear from Dr. Hess.

It is good to see you again, sir.

STATEMENT OF DR. EARL H. HESS, PRESIDENT, LANCASTER LABORATORIES, INC., LANCASTER, PA.

Dr. HESS. It is nice to see you. I appreciate this chance to follow-up on my testimony of some months ago.

As indicated, I expect that my entire testimony will be entered into the record. I would just like to page through and highlight it in order to try to stay within that 5-minute limit.

The personal background of myself, Lancaster Laboratories, and so forth, I will not read. I would rather move directly to three items which are basic and need to be discussed in advance of the specific comments I will have on the proposed legislation. These begin on page 3 of my testimony under the title of "Government Reliance on the Private Sector."

As you are well aware, Senate Joint Resolution 93, as well as Senator East's bill, S. 2278, addressed issues of very keen importance in the area of Government competition. This section of my testimony attempts to summarize that material, but also describes some recent legislative developments which are very disappointing to us, namely, those amendments to the DOD authorization bill which run directly counter to the reliance on the private sector philosophy which we assumed and hoped was the Reagan administration's real thrust.

I point out that the trend emplified by the addition of 17,000 new Government employee slots can make the whole subject of the details of Government procurement rather academic; there won't be any!

I move then to another subject. I may sound like a broken record on this one, because every time I testify something is said about small business and the unfair competitive advantage that the nonprofits hold. I have not coined the words "commercial nonprofits". Rather, Dr. Hansmann from the University of Pennsylvania Law School uses that term.

I try to set forth in my testimony the simple fact that we forprofit small businesses cannot compete with nonprofit organizations in the procurement process unless we are grossly more efficient than they. It is the only way to counterbalance the tax advantage and other benefits that they have.

On the other hand, this country cannot afford the inefficiencies permitted the commercial nonprofits by this system. I relate directly to the specific area of laboratory services where the problem is particularly keen, and has been for years and years.

I cite an example of a contract we just lost to the University of Missouri which has nothing to do with research. It is repetitive testing. We have been underbid. I can offer you more detail on that, if you have an interest.

My testimony points out that there are positive and constructive things that can be done by giving some examples within the Pennsylvania community of the Pennsylvania technical assistance program [PENNTAP].

My third concern relates to the SBA size standards. I will spend very little time on this—only to say that just about the time my business is coming to the point where I may have the muscle to struggle with Government procurement, I realize that by having 10 more people I would be classified as big business and, therefore, excluded from the small business procurement provisions which we are talking about today under the proferred new size standards. We ask that the Senate Small Business Committee look carefully at the comments submitted to SBA by the small business community before these size standards are finalized.

With respect the Small Business Procurement Reform Act of 1982, my written statement deals with two issues. The first issue suggests that full disclosure of circumstances should be made where a sole source contract is awarded or where a geographic restriction is placed.

This is all well and good if quality of service or product can be closely defined. I support that concept.

However, those of us providing professional services oftentimes have a problem defining precisely quality of service, and therefore, the Government is oftentimes shortchanged by going with the low bidder. I try to make that point as a qualifier to my basic agreement with the concept of open bidding.

With respect to the "unbundling" aspect of Government contracts, I again applaud the principle and say that I think there is a lot that can be done in that area. I also offer the alternate of required subcontracting by large prime contractors as a way of accomplishing the intent of the legislation.

My written statement concludes with a section in which I do talk specifically about some positive things that already happened. The Small Business Innovation Act and the prompt payments legislation have been very real and important to me.

Senator **HAYAKAWA**. Thank you, Dr. Hess.

You will be interested to know that this committee is reviewing the proposed changes in the SBA size standard regulation for your industry, namely, research.

Dr. **HESS**. I appreciate that very much. It is good to appear before you.

Senator **HAYAKAWA**. We will come back to some questions later.

[The prepared statement of Dr. Hess follows:]

STATEMENT OF DR. EARL H. HESS, PRESIDENT, LANCASTER LABORATORIES, INC.

My name is Earl H. Hess. I am president of Lancaster Laboratories, Inc., of Lancaster, PA. On behalf of the 200,000 Pennsylvania small businesses that I represent here today, I salute our fellow Pennsylvanian, Senator Specter and the co-sponsors of S-2446. Their concern for small business, and their desire to increase opportunities for small businesses to contract with the Federal Government are commendable. Reform of Federal procurement policy is badly needed. If achieved, it would yield at least two major benefits. Firstly, such reform would enable small business to widen its markets at a particularly critical time. Secondly, it would save the Government money, because of the greater efficiencies typical of small, for-profit businesses. The importance of efficient utilization of Federal resources is painfully obvious in our day.

Lancaster Laboratories, Inc. is a small research, development and analytical services firm which I established in 1961. Beginning with three persons, our company has grown steadily to a present staff of 67, nearly half of whom are degreed professionals, mostly in the fields of chemistry and biology. We opened a branch laboratory in Waynesboro, PA in 1978. Attached to this testimony is a one-page scope sheet describing the services which Lancaster Laboratories provides. In our 21 year history, we have never laid off a person for lack of work. Further, during the last two years, we have committed about $800,000 to expanded facilities and new equipment. Only a small percentage of our total business has been with Government, not because Government doesn't need laboratory services, but because Federal procurement policies discriminate against small for-profit businesses and because bureaucratic red tape has discouraged us from aggressively pursuing Government business.

My negative attitude toward Government contracts is shared by many of my peers in small business. I am most familiar of course with the independent laboratory field. There are several thousand of these laboratories in the U.S., the vast majority of them small businesses. These firms are part of that group of small high technology businesses which many studies have found to be the most fruitful generators of innovative products and processes.

My national perspective on the unique procurement problems of independent laboratories has been gained through my experience as Director of Government Relations for the American Council of Independent Laboratories Inc. (ACIL), the professional association of independent engineering and scientific firms most of which are small businesses.

In recent years, my involvement with Chambers of Commerce at the local, state and national level has increased my appreciation of the problems of a broader range of small businesses. I serve on the U.S. Chamber's Small Business Council, am Chairman of the Pennsylvania Small Business Advocacy Council (PASBAC) a division of the Pennsylvania Chamber, and also serve as Vice Chairman, Public Affairs, of the Lancaster Chamber of Commerce and Industry. I am also a member of the Action Council of the National Federation of Independent Business (NFIB).

In 1979, I served on an SBA, Office of Advocacy Task Force that studied the problem of Government competition with small business, a subject closely associated with the small business procurement concerns being addressed today. I have testified before House and Senate Committees at least four times in the last two years on the subject of Government competition and welcome today the opportunity to relate that critical issue to the procurement process.

Before addressing the specific procurement reforms proposed in S-2446, I want to address some fundamental issues.

GOVERNMENT RELIANCE ON THE PRIVATE SECTOR

The foundation of a healthy relationship between Government and small business is an effective policy of reliance on the private sector for appropriate goods and services. This policy, embodied in OMB Circular A-76, has been in the books for decades. Several initiatives within the past two years have reinforced it. A key element of this Administration's stated economic recovery plan has been reduction in the size of Government, at least in part, through greater reliance on the private sector. Two pieces of legislation, the Hayakawa-Drier Resolution (S.J. 93, H.J. 294), and the Economy in Government Act of 1982 (S-2278) have been introduced during this session of Congress. The former simply would give present OMB policy legislative muscle. S-2278 goes further in dealing with the distinction between for-profit and non-profit entities in the procurement process. I should note that my testimony with regard to each of these bills is already on record.

These were certainly encouraging developments to small businessmen like myself. However, events of recent months have turned our hopes to disappointment. S.J. 93 and S-2278 are being ignored in committee, and the anticipated forceful interpretation and implementation of A-76 by the Administration have not materialized. Meanwhile, major restrictions on contracting out are being placed on the Department of Defense through amendments to authorization legislation. In August, Congress passed S-2248, which includes one provision adding 17,000 additional manpower spaces to DOD's civilian personnel ceiling, and other provisions that severely restrict DOD's ability to contract out to private-sector firms. Even this very week, the House is considering "military pay" legislation which would further restrict contracting to private sector firms. If Congress continues to pursue this philosophy, the whole subject of procurement policy reform will become academic! Federal agencies should be required to justify why an activity should be performed by Federal employees rather than having to justify the performance of an activity by the private sector.

COMPETITION FROM NOT-FOR-PROFITS

Another sore point with small businessmen is the problem of unfair competition from "commercial" not-for-profit organizations. As our SBA Task Force learned, this kind of unfair competition is prevalent both in Federal procurement and in the private marketplace. In the real world of many small businesspersons, the simple fact is that the largest threat we face is the invasion of our markets, not by big business or new small businesses, but by non-profit organizations (all too often educational institutions) that have been allowed by their administrators to stray from their traditional public service role into commercial, proprietary markets. The edge such entities enjoy is not quality of work or efficiency of operation; it is an unfair tax advantage. Statutes relating to this issue are vaguely written and fuzzily interpreted by IRS and the Treasury Department. As a result, legitimate for-profit small businesses are being squeezed out by less efficient and less innovative non-profits. Further, the Government and the public are being denied the tax revenues that small business would produce and the fruits of their innovative efforts.

It is particularly distressing for me to see this very thing happening in my areas of applied research and development, commercial testing and technology transfer. It is happening with the blessing of Government and with supplementary grants to non-profits which further widen the competitive gap, all in the name of meeting an urgent national need through "University-Industry-Government cooperation." Presently in Pennsylvania, such a program is being touted under the name of Project Ben Franklin. It will use my tax dollars to foster increased encroachment of publicly funded institutions into the commercial world, without concern about the adverse impact of such programs on small, innovative, high-technology service businesses.

Indeed, for me the problem of commercial activity by non-profits is very present. Just two days ago, we attended a debriefing that we had requested at the National Cancer Institute, to try to learn the rationale for award of a specific NIH contract to The University of Missouri. This procurement involves the repetitive testing of rat feces for pathogenic organisms. It has no educational or research dimension to justify its performance by a publicly funded institution.

The Economy in Government Act of 1982, introduced by Senator East and co-sponsored by many of the promoters behind S-2446, deals very responsibly with the non-profit problem in Federal procurement. I would hope that those features within that proposed legislation will be incorporated into any final procurement reform legislation.

Recently I had the opportunity to review articles by Professor Henry B. Hansmann of The University of Pennsylvania Law School entitled "Reforming Non-Profit Corporation Law" and "The Rationale for Exempting Non-Profit Organizations from Corporate Income Taxation." Dr. Hansmann's work is part of the study of the role of non-profits in our society carried on by the

Institution for Social and Policy Studies at Yale University. Dr. Hansmann contends that tax exemption is necessary for the non-profit as a tool for capital formation, but he also makes a strong point for stricter limitations in granting non-profit status. Using mathematical models, Dr. Hansmann demonstrates how "commercial" non-profits can squeeze for-profit firms out of any commercial market, and that the only defense of the for-profit is its greater operating efficiency. Gentlemen, our economy cannot stand the replacement of efficient, innovative, revenue- and job-producing small businesses with non-profits which attain their position of market dominance through unfair advantage. To avoid this, the unfair competition of non-profits with small for-profit businesses in the provision of commercial goods and services must cease.

It is not my intention that these strong statements be interpreted as a broad indictment against non-profits or non-profit status. Indeed I am closely associated with many which serve very significant public service functions. Many non-profits have established guidelines with respect to commercial activities and monitor them closely. For example, the Pennsylvania Technical Assistance Program (PENNTAP), operated by Penn State University and on whose Advisory Council I have recently served, has well-defined guidelines. In fact, just yesterday eight PENNTAP specialists spent the day with our scientists exploring our respective roles in technology transfer in the interest of more effective cooperation.

SBA SIZE STANDARDS

Efforts by the SBA during the last several years to revise size standards used in defining "small business" for purposes of procurement have threatened many of us in the small business community and have even disturbed

SBA's own Office of Advocacy. Apparently in the interest of "cottage industry" segments of various SIC categories, SBA is proposing to reduce drastically the employee-size ceilings that define small businesses. If this initiative succeeds, both Government and small business will be losers. Incredible as it might seem, under the present SBA proposal, with 10 more employees Lancaster Laboratories would no longer be a small business. Firms like mine would then be denied the special procurement opportunities afforded small businesses. And the Government would be left with a plethora of two- and five-person businesses that are really nonentities when it comes to Government contracts. I would strongly urge members of the Senate and House Small Business Committees to monitor this situation closely and to review the comments submitted by small businessmen to SBA on the subject of size standards redefinition.

OVERLY COMPLEX AND UNREASONABLE PROCEDURES

A number of small business criticisms of the Federal procurement system can be categorized as "overly complex and unreasonable procedures." These include:

- Excessive demands that require bidding two and three times on the same proposal.
- Lengthy requests-for-proposal filled with jargon and complicated terms and stipulations which bury key information.
- "Call-order contracts," into which a firm puts much up-front time, effort and money can be summarily - and seemingly arbitrarily - terminated by the Government well before completion.
- Requirement of repeated price justifications from the Government, over and over, for the same work.

Government regulation of contractor costs that discourages cost-efficient performance, often leads to an adversarial relationship between buyer and seller. The issue should be the price the Government pays, not the contractor's internal cost operations. The delay in final payments pending a final audit and the time and effort associated with that audit represent unnecessary and unproductive overhead when a contract has been negotiated on a fixed fee/unit basis. Much more could be said on this subject. Let it suffice to conclude that the more procurement procedures can be simplified and streamlined, the more small businesses will show an interest in Government contracting.

PROCUREMENT REFORM ACT OF 1982

Now, I will address specific proposals of S-2446, the Small Business Procurement Reform Act of 1982. The section requiring full disclosure of circumstances wherein a sole-source contract is awarded or where a geographic restriction is placed on the bidder is obviously intended to promote open competition and free market access to the broadest base of offerers. This is indeed a worthy objective and one that I fully support. There is. however, one precaution that I would like to offer. All business transactions need to be built on the foundation of quality and price. Wherein quality is readily defined and monitored as part of the procurement process, the major deciding factor should indeed be price. But when quality cannot be defined in a straightforward manner (e.g. the provision of many professional services), contract awards based on price alone can be counterproductive. A poor quality service or product at whatever the cost, does not fulfill the Government's need; further it frustrates the legitimate bidder, so that in time he will simply ignore solicitations from the Government.

Our laboratory has one of the most sophisticated computerized cost accounting systems in operation within any small business, so that I have very precise knowledge of our operating costs. Furthermore the growth record of our business in recent years attests to the fact that we are very cost competitive with other quality laboratory service organizations in the commercial marketplace. Yet our experience in Government procurement is such that we rarely, if ever, respond to an IFB, because of the nearly zero chance of receiving the award. Indirectly, that tells me something about the quality of services being obtained by the government through a strictly low bid process. Fortunately, there is another procurement mechanism, the Request For Proposal (RFP). A response to an RFP is usually made in two parts, a technical section and a business section. Only those offerers whose technical proposals rate high are considered for review of their cost proposals. Such a mechanism is in theory much better, but we have found many inequities in actual practice. In summary, procurement policies that promote open bidding are commendable if the procurement officer has a true hold on quality of product or service. Otherwise, low bid is meaningless.

Moreover, we have been informed many times by technical people within the government who are not happy with the performance of a low bid awardee that it is too costly and almost impossible from a practical legal standpoint to get rid of the poor performer. The usual course of action is to wait until the next yearly contract is let and to try to disqualify the firm from being considered again.

A section of S-2446 deals with "Component Bidding on Large Systems Procurements". Again, the goals of this proposed legislation are commendable. I am convinced that there is much "unbundling" of procurement packages that could be done conveniently. This would provide small businesses access to new markets and also would introduce a new and tough competitor (the small businessperson) to the scene, thus resulting in cost savings to the taxpayers. Such procurement regulations could, however, be pushed to an extreme that would be counterproductive, by adding to procurement red tape, and increasing costs to the taxpayer. There is an alternate mechansim for accomplishing the stated purpose, namely, the requirement that large prime contractors sub-contract reasonable percentages of given projects to small businesses. Such a mechanism is set forth in Public Law 95-507, but it lacks the muscle to insure that prime contractors follow its guidelines. It would be my recommendation that the problem of small business access to large procurements be addressed by requiring "unbundling" where practically feasible, and where not, by requiring appropriate small business subcontracting by the large prime contractor.

I have little substantive comment regarding the provisions of the bill with respect to arbitration panels and advisory committees. I am in favor of arbitration as a means of expediting the resolution of disputes and the latter as a means of providing the bureaucracy with some real world-input. I am opposed to committees and panels that simply abet bureaucratic inertia.

POSITIVE ACCOMPLISHMENTS

I would be remiss if I did not point out two very positive accomplishments of this Congress with respect to small business procurement. I refer to prompt payments legislation and the enactment of the highly controversial Small Business Innovation Research Act (HB-4326). With respect to the latter, I can report that our Company has participated in the Model Small Business Innovation research program of the National Science Foundation with excellent results. For a Government investment of less than $25,000 a significant break-through in asbestos detection methods was discovered. The work has been published and follow-up studies are anticipated. Through passage of HR-4326, the reputation of the small business community is at stake, but I have no fears that implementation of this legislation will prove highly beneficial to the Federal Government. With current interest rates and the cash-poor position of many small businesses, the value of the prompt payments legislation is obvious. I commend the members of the Congress, especially of the Senate and House Small Business Committees for their support of small business in these two key areas.

Mr. Chairman, I believe that the time has come for Congress, Federal agencies and the small business community to join together in a careful review of Government procurement policies and procedures. It is my opinion that we need to examine first of all some premises basic to our free-enterprise, democratic system: (1) the policy of reliance on the private sector; (2) the proper role of for-profit and non-profit organizations in the provision of goods and services; and (3) the need for our procurement process to get back to the basics. S-2446 represents a significant step in that review. Today's Hearing will doubtlessly reveal that some of the bill's provisions should be strengthened and clarified. As I have done, I'm sure others will suggest additional provisions that should be added to S-2446 perhaps through merger with other proposed legislation. For now, however, the important thing is to get started. This legislation is an important first step.

I congratulate Senator Specter for his leadership in this area, and I hope that the Senate Small Business Committee will proceed without delay in further consideration of this bill. Thank you for the opportunity to express my views. I hope they will be helpful.

Lancaster Laboratories
INCORPORATED

Main Laboratory
2425 NEW HOLLAND PIKE • LANCASTER, PENNSYLVANIA 17601
(717) 656-2301
Franklin Division
5424 BUCHANAN TRAIL EAST • WAYNESBORO, PENNSYLVANIA 17268
(717) 762-9127

Earl H. Hess, Ph.D., Pres. • Fred R. Albright, Ph.D., V.P. Tech. Dir. • James P. Dux Ph.D., Sr. Tech. Associate, Marketing Mgr.

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CERTIFICATIONS AND REGISTRATIONS

Water Analysis (EPA #38-037) Pennsylvania Dept. of Agriculture and USPHS-Dairy Product Testing and Farm Inspection, Food and Drug Administration Reg. #25-13291 U.S. Dept. of Agriculture Certification—Meat Analysis (#4282), American Association for Laboratory Accreditation (#1, Chemistry) Bureau of Mines Small Operator Assistance Program

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MEMBERSHIPS
(Laboratory or Staff)

American Council of Independent Laboratories, Inc., American Association of Small Research Companies, Pennsylvania Manufacturing Confectioners' Association (Associate Member), Lancaster Chamber of Commerce & Industry, Better Business Bureau, Institute of Food Technologists, American Chemical Society, American Association for the Advancement of Science, American Society for Testing and Materials, American Oil Chemists Society, New York Academy of Sciences, Association of Official Analytical Chemists, Pennsylvania Approved Dairy Laboratory Directors Association, American Water Works Association, National Federation of Independent Businesses, American Association for Laboratory Accreditation, Pennsylvania Chamber of Commerce, U.S. Chamber of Commerce, American Industrial Hygiene Association, American Public Health Association, Water Pollution Control Federation.

Senator HAYAKAWA. Shall we proceed to Mr. Hahn?

STATEMENT OF BRUCE N. HAHN, MANAGER OF GOVERNMENT AFFAIRS, NATIONAL TOOLING AND MACHINING ASSOCIATION, ACCOMPANIED BY PAUL SEIDMAN, COUNSEL

Mr. HAHN. Thank you very much, Senator. It is very nice to be with you here today.

I am Bruce Hahn. I am manager of Government affairs for the National Tooling and Machining Association. We represent 14,000 small businesses. Our members are almost exclusively small businesses. They have an average size perhaps of 20 employees, and they are found in all the industrial States in the United States, including a heavy concentration in Connecticut, California, and Illinois, including one of our members who used to be your roommate, Senator Dixon.

Our members would like to participate in contracting to a much greater extent than they are now.

I think I would prefer, if I may, to address the overall picture and then perhaps make a couple statements on specific issues.

The current state of small business' participation in Federal procurement is dismal. Just in the area of spare parts alone, simple spare parts, something that virtually any of our members might be able to make, 7 percent I believe is the figure which is competitively bid right now. Ninety-three percent are not competitively procured.

There is a system of barriers and restrictions which make it virtually impossible, or at least make it very, very difficult, for a small businessman without the administrative resources to be able to participate in procurement in the Federal Government.

There are several very sad implications as a result of this. The Government buys something like $10 billion worth of spare parts every year. This is just spare parts. We are not talking about major systems.

In a study performed by SBA and later reconfirmed in a very recent report by the GAO, it has been estimated that 40 percent could be saved when they took contracts that previously had been sole supplier and competitively bid them. Our members are ready; they are able; they are willing, and they would like to help the Government save billions of dollars.

However, there are a variety of restrictions. Another side of this issue is the implication of these Federal policies to the industrial base of the United States. To the extent that small businesses, many thousands of small businesses, are excluded from participation, their ability to support our industrial base and our defense industrial base is greatly weakened.

It was to a large extent during the Second World War small businesses in our industry that were able to gear up in a manner that was unheralded and unequaled in the entire history of the western world to produce the defense armaments that we needed quickly. We are losing that base. Therefore, there is good reason for small business participation in defense contracting.

We very much appreciate Senator Specter, Senator Dixon, and Senator Hayakawa, and the many others who have introduced and cosponsored S. 2446. We think this bill is one that was introduced with the best intentions. We think what it is trying to achieve is good. However, there are a number of suggestions that we would make in terms of technical changes which we believe would strongly improve it. We strongly support your efforts thus far. We would be more than willing to work with you further in suggesting further improvements. We believe that the start which has been made by this committee is very, very laudable.

Another area outside of S. 2446, something which this committee might get into and might consider reviewing, is in the area of spare parts procurement policy. Right now small businesses, as I mentioned earlier, have a tremendous difficulty in becoming eligible to participate. They have to go through a variety of hoops.

The SBA was originally charged with responsibility for determining responsibility; in other words, determining whether or not a small business would be capable of being able to perform on a specific contract.

That system has been duplicated. The Air Force and many of the other branches of the military have their own systems. They have no statutory basis, and, indeed, many people believe they are legally questionable. The bottom line is that 93 percent of your contracts are not competitively bid. There are, especially in the economy we have today, plenty of companies that are ready, willing, and able to contribute to our industrial base, to reducing our military budget, and we would like the opportunity to be able to contribute to that.

Thank you very much, Mr. Chairman.

Senator HAYAKAWA. Thank you, Mr. Hahn.

[The prepared statement of Mr. Hahn follows:]

TESTIMONY OF THE NATIONAL TOOLING & MACHINING ASSOCIATION

My name is Bruce N. Hahn and I am Manager of Government Affairs for the National Tooling & Machining Association. Our members are very interested in small business procurement because a large number are presently DOD subcontractors. While a few do some prime contracting, all of our members would certainly like to see a change in the present non-competitive system that prevents most of them from competing.

The National Tooling and Machining Association represents the tool, die and precision machining industry. This industry is composed of 14,000 independent contracting manufacturing plants, almost all of which are small business concerns. These companies build special tools, dies, jigs, fixtures, molds, gauges, special machines (automation, robotics, and production lines) and precision machined parts or components. They use a wide variety of equipment and processes, including most machine tools from the simplest lathe to the most complex numerically-controlled machining center, electrical discharge machining, electrical-chemical milling, and electron-beam welding. They commonly achieve tolerances to one-ten-thousandths of an inch and regularly use computers as an aid in design, machining, and control of operations.

NTMA appreciates the opportunity to testify on S. 2446, the "Small Business Procurement Reform Act of 1982." Many of our members are unable to effectively compete for DOD contracts they are capable of performing at a fraction of the prices presently paid. We believe that legislation such as S. 2446, with technical modification, is a step in the right direction and we commend Senator Specter for introducing it. Removing barriers to small business competition will not only result in small business receiving a greater share of the Federal procurement dollar, but also, significant dollar savings to the taxpayer and a greater degree of defense preparedness.

Our testimony today will address the provisions of S. 2446 and also provide additional suggestions for reforming the procurement system.

I. S. 2446 — The "Small Business Procurement Reform Act of 1982."

Briefly stated, S. 2446 would:

1. Improve Commerce Business Daily notification to Small Business of proposed procurements;

2. Direct each agency to break its large system procurements, whenever practicable, into smaller components in order to give small businesses a greater opportunity to compete;

3. Authorize the Small Business Administration to establish arbitration panels to resolve minor contractual disputes; and

4. Establish a Small Business Procurement Advisory Committee to advise the Congress and the Administrator of SBA on matters relating to small business procurement.

Each of these points will be addressed in detail below.

A. Minimum Solicitation and Award Standards.

As highlighted in recent hearings conducted by this Committee, inadequate and untimely Commerce Business Daily notification have been a significant barrier to small business participation in the procurement process. As a result of these hearings, the Senate enacted S. 1947. S. 1947 would require that a synopsis be published in the Commerce Business Daily at least 15 days before a solicitation is issued and that once issued that competition not be foreclosed for at least 30 days.

For technical reasons, we prefer S. 1947 to S. 2446. The separate time periods for advance synopsis of a solicitation and for keeping a solicitation open for competition in S. 1947 are to small businesses' advantage. S. 2446 would permit an award 45 days after CBD synopsis even though competition may have been foreclosed at a substantially earlier date. For example, under S. 2446, a procuring agency could establish the day after CBD synopsis as the cut-off date for the receipt of bids as long as an award was not made until 45 days later.

B. Component Bidding on Large Systems Procurements.

S. 2446 would require each Federal agency to " . . . review its procedure for awarding procurement contracts for large systems on which small business concerns cannot compete, and take all practicable steps to subdivide the procurement contracts into smaller components on which small business concerns can compete." A similar policy statement was enacted by the 1980 White House Conference on Small Business./1

However, something usually gets lost in translation between broad policy statements and implementation. Such a policy statement on component breakout is already contained in the Defense Acquisition Regulation/2 and has had little impact.

S. 2446 also does not address the $10 billion in spare parts contracts for

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1/ Recommendation 27 "Procurement agencies should break down large requirements (including those for research and development) into smaller parts where feasible to permit solicitation from, and award to, small businesses."

2/ DAR § 1-326

major systems that DOD awards on a noncompetitive basis to large original systems manufacturers. DOD's legally questionable method of procuring spare parts not only prevents small business competition, but also results in DOD spending billions more than if these contracts were competed. Because of the importance of this issue to both small business contractors and the taxpayer, we will address this problem in some length.

1. The Legally Questionable DOD Breakout Regulation

The most significant barrier to small business participation in DOD spare parts contracts is a directive entitled "Department of Defense High Dollar Spare Parts Breakout Program" March, 1969, commonly known as the Breakout Regulation./3 One would think from the phrase "Breakout Program" in the title that the intent of the directive was to promote, rather than restrict competition. However, the title is a misnomer. The directive restricts, rather than encourages, competition. It is a legally questionable system of bidder prequalification that deprives small businesses, such as NTMA member companies, of their statutory right to have SBA make the final determination as to their capability to perform a particular contract. As surprising as it may seem, the restrictive codings which are the basis of this prequalification system are often the result of recommendations from original systems manufacturers who are in an obvious conflict of interest situation.

a. Bidder Prequalification as a Means to Screen Out Small Firms. The Certificate of Competency Program — In General

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3/ The Army refers to the regulation as AR 715-22; Navy NAVMATINST 4200.33A, Marine Corps MCO P4200.13A, Air Force AFR 57-6 and the Defense Logistics Agency as DSAM 4105.2. All are identical.

In order for a firm to be awarded a Government contract, a determination must be made that it is responsible. Responsibility is the ability of a firm to perform a particular contract. As a general rule, the contracting officer has the authority to make the final determination as to a firm's responsibility. However, under the Small Business Act, small business concerns have the right to have SBA make the final determination as to their responsibility, if they would have been awarded a particular contract except for a contracting officer's negative responsibility determination./4 This review is conducted under SBA's Certificate of Competency program.

The enactment of certificate of competency legislation was a result of the systematic exclusion of small business from defense contracts during World War II. Testimony in 1942 hearings before the Senate Banking and Currency Committee showed that contracting officers often refused to make awards to small business concerns on grounds that they were not responsible. They would subsequently discover that the same small businesses were performing the work as subcontractors to the large firms awarded the contract in question. The War Production Board also called for the enactment of legislation to correct the tendency of contracting officers to underestimate the capabilities of small business concerns and the resulting negative impact on the industrial base./5

b. The Use of Bidder Prequalification to Deprive Small Firms of the Right to Apply for a COC

The current fiasco in spare parts procurement results from an artifice used by DOD that deprives small business concerns of their right to have SBA make the final

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4/ 15 U.S.C. § 637(b)(7).

5/ Senate hearings on S. 2250, 77th Congress, 2nd Session.

determination as to their responsibility. This is done by a system of bidder prequalification set forth in the so called Breakout Regulation. The concept is fairly simple. If a small business is precluded from bidding by a bidder prequalification system, the need to refer the question of their responsibility to SBA for Certificate of Competency purposes never arises. It is DOD's position that a small business is only entitled to a certificate of competency review if it would have been awarded a particular contract if it were not for the contracting officer's negative responsibility determination. If a small business is precluded from bidding, this stage of the procurement process is never reached.

The way this is done is by the assignment of procurement method codes (PMCs) that restrict the award of contracts for spare parts to sources that have prequalified. One of the assumptions underlying the PMCs is that procurements should be restricted to prequalified sources on the grounds that it is necessary to assure the reliability of a part. Yet this has absolutely nothing to do with quality control. Quality control is imposed by more vigorous specifications and inspections in cases where the part is critical. Inspections must be performed on the product to ensure quality control regardless of whether the supplier is small or large. Larger companies have no better equipment, only more equipment and it is incorrect to assume that they are somehow better prepared to produce quality products. In fact, most parts with restrictive PMCs are subcontracted to small businesses, put in a box with the original systems manufacturer's name, and marked up before being delivered to DOD.

Other grounds for restrictive codes are that unique manufacturing capabilities are needed, that adequate data to produce the part is not available or that there is a question as to whether or not the Government has the right to use the data necessary to produce the item in question.

A similar system of bidder prequalification was held to violate the Small Business Act in Office of Federal Procurement Policy's Uniform Films Production Contracting System/6. More specifically, GAO held in that case that a determination that a small business was not qualified to participate in federal audio-visual contracts under OFPP's Uniform System for film and videotape production violated Small Business Act provisions giving small firms the right to have SBA make the final determination as to their capability to perform.

c. Original Systems Manufacturer Participation in Assignment of Restrictive Procurement Method Codes

The original systems manufacturer plays a significant role in the assignment of PMCs. Under the DOD High Dollar Spare Parts Breakout Regulation, the original systems manufacturer provides DOD with contractor recommended codes (CRCs). These CRCs may restrict the procurement of a spare part to the original systems manufacturer. A large number of the CRCs are adopted by the Defense Department as PMCs. To say the least, the participation in the assignment of PMCs by original systems manufacturers that stand to benefit from restrictive PMCs raises serious conflict of interest questions. As some SBA personnel have said, this is like letting a rabbit loose in a carrot patch.

d. Abuses in Assignment of Restrictive Procurement Method Codes

Not surprisingly, there have been significant abuses in the assignment of

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6/ 60 Comp. Gen. 104, B-198360, 80-2 CPD ¶ 419.

procurement method codes. A multitude of items restricted on the grounds that unique manufacturing capabilities are needed could be made at a significant savings to the Government by smaller companies. The tragedy is that a high percentage of these same items are presently produced by smaller companies on a subcontract basis and marked up, in some cases hundreds of percentage points, in the final price paid by the Government.

e. DOD's Rulemaking Effort

DOD has recently solicited comments on proposed revisions to the Breakout Regulation. However, just as the present directive the DOD proposal contains a legally questionable system of bidder prequalification with restrictive codes resulting in sole source procurements assigned as a result of the recommendations of the original systems manufacturer.

In conducting this rulemaking effort, DOD has not only ignored the procedural requirements of the Small Business Regulatory Flexibility Act, but has not even published its proposal in the Federal Register.

2. The Result — Increased Cost, Diminished Small Business Opportunities, and Erosion of the Defense Industrial Base

a. A Recent SBA Study Shows Potential for Saving Billions of Dollars by

Eliminating Present Restrictive Practices

As a result of DOD's restrictive procurement practices, original systems manufacturers have taken advantage of their sole source status by charging the Government premium prices for spare parts. Our members have told us that as a rule, they can profitably sell high quality spare parts at one-third to one-half the price presently paid by the Government. These claims are corroborated by a September 4, 1981, SBA study prepared at the request of the House Small Business Committee of cost savings realized when 181 parts were converted from sole source to competitively bid./7 The study showed a savings to the Government of $6.7 million for these 181 parts over a period of approximately one and one-half years, a savings of 38.5% of prices previously paid. The 181 parts broken out are a drop in the bucket compared to the 3.9 million spare parts presently purchased by DOD. Of these 3.9 million spare parts, the study notes that only 300,000 or 7.9% are presently purchased on an openly competitive basis, leaving more than 3.6 million parts for future potential breakout. If these 3.9 million spare parts, which cost the Federal Government about $10 billion per year, were competitively bid and the savings approximated those in the SBA study, the Federal Government could get the same products for about $4 billion less and the savings could reduce the federal deficit by that amount. Furthermore, in a study recently conducted at the request of the House Small Business Committee, GAO concluded that SBA may have understated the potential for savings. /8

b. DOD Practices Result in Diminished Small Business Opportunities

Highly qualified small businesses are also deprived of a multi-billion dollar

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7/ The study is published as part of the record in Small Business and the Federal Procurement System, Hearings Before the Subcommittee on General Oversight of the House Committee on Small Business, 97th Congress, 1st Session, 415, 422-436 (1982).

8/ SBA's Breakout Efforts Increase Competitive Procurements at Air Logistics Centers, (GAO/PLRD-82-104), August 2, 1982.

market. Although many small companies presently manufacture spare parts as subcontractors, this arrangement leaves them at the mercy of large original systems manufacturers. The large original systems manufacturers generally take such contracts in-house when business is slack to maintain their workforce. Aside from skirting Small Business Act provision relating to Certificates of Competency, such action hardly seems consistent with the Small Business Act statement that "It is the declared policy of the Congress that the Government should aid, counsel, assist, and protect, insofar as possible, the interests of small-business concerns in order to preserve free competitive enterprise, to insure that a fair proportion of the total purchases and contracts and subcontracts for property and services for the Government . . . be placed with small-business enterprises."/9

c. DOD Practices Contribute to Lack of Industrial Preparedness

Another result of this questionable mode of purchasing aircraft spare parts is the present sorry state of our defense industrial base. In a December 31, 1980, report entitled "The Ailing Defense Industrial Base: Unready for Crisis," the Defense Industrial Base Panel of the House Armed Services Committee pointed out that the private sector would be unable to surge production in order to respond to a national emergency. It is also a well known fact that as a result of present long lead times for spare parts, the Air Force has been cannabilizing planes to keep others operational./10 Aside from the billions that would be saved annually by eliminating the sole source procurements sanctioned by the Breakout Regulation, the development of alternative sources of supply would significantly strengthen this nation's capability to respond in time of

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9/ 15 U.S.C. § 631.

10/ Mossberg, Out of Action: Many Air Force Planes Often Can't Be Flown for Lack of Spare Parts, Wall Street Journal, June 1, 1982, page 1.

crisis.

C. Government Procurement Contract Arbitration Panels.

S. 2446 would authorize the Small Business Administration to establish arbitration panels to resolve contractual disputes between the procuring agencies and small business concerns. Use of such panels would be voluntary and a decision of such a panel would be binding only to the extent that the concern and the agency agree that such a decision would be binding.

Disputes between procuring agencies and contractors are of two types: (1) pre-award disputes concerning who a contract should be awarded to; and (2) disputes concerning contract performance. Because of the expense of litigation in federal courts, most pre-award disputes are presently decided by the General Accounting Office. In our judgment, GAO has not provided an adequate forum for aggrieved bidders. GAO must wait for an agency response to a bid protest before rendering a decision. Procuring agencies routinely fail to respond to bid protests in a timely fashion. There is no incentive for them to do so. GAO has no authority to prevent a contract award and generally by the time the agency responds to a protest and a decision is issued, the contract in question will have been awarded and substantially performed, thus leaving the successful protestor in the position of having won the battle but lost the war. The solution to this problem is not creating arbitration panels that would also lack the authority to compel agency responses and enjoin procurements. A better approach would be to give such authority to GAO.

As far as disputes concerning performance are concerned, Congress has already addressed the problem of claims submitted by small business contractors in the Contract Disputes Act of 1978, Public Law 95-563, which provides simplified procedures before Boards of Contract Appeals for small claims. Under the expedited procedure, which is available for claims of $10,000.00 or less, the Board will, use simplified procedural rules and whenever possible, issue a decision within 120 days after it receives written notice of a contractor's election to utilize such procedures./11

Under accelerated procedures which are available for claims of $50,000.00 or less, a decision is to be issued, if possible, within 180 days after such an election is made./12

The Boards of Contracts Appeals already have the expertise and the statutory mandate and, in our opinion, nothing would be gained by transferring such authority to a new, untrained bureaucracy at the Small Business Administration. We would also like to note that the Contract Disputes Act contemplates the Office of Federal Procurement Policy periodically adjusting the dollar threshold for the simplified procedure for under $10,000.00 claims for inflation./13 Although we have undergone a considerable period of inflation since the 1978 enactment of the Contract Disputes Act, this has never been done. It would be a positive development for small business concerns if the Committee would urge OFPP to comply with the Contracts Disputes Act of 1978 and adjust the dollar threshold at this time to take into account the runaway inflation of the past 5 years. Legislation should be enacted giving OFPP the authority to adjust the dollar threshold for expedited procedures presently available for claims of less than $50,000.00.

11/ 41 U.S.C. § 608.

12/ 41 U.S.C. § 607(f).

13/ 41 U.S.C. § 608(f).

D. Small Business Procurement Advisory Committees.

S. 2446 would provide for the establishment of a Small Business Procurement Advisory Committee to advise the Congress and the Administrator on small business procurement issues. In our experience, advisory committees have engendered great expectations and little results. If such a committee were formed, it should be staffed on a non-partisan basis with small business advocates, based upon technical competence. If its recommendations were not filed away without being read, as those of advisory committees often are, the establishment of such a committee may have a positive impact.

II. Other Possibilities for Reform

1. Enact a clarifying amendment to the Small Business Act that eliminates the breakout regulation as a means for DOD to avoid the Certificate of Competency process and requires the SBA to issue COC's for under $10,000.00 contracts.

The high-dollar spare parts breakout regulation is nothing other than an artifice which deprives small businesses of their right to have SBA make the final determination of their capability to perform. As previously noted, legislation giving small businesses this right was enacted because of a tendency of contracting officers to underestimate the capabilities of small business concerns and the resulting harm to the defense effort. This rationale is as pertinent today as when the Certificate of Competency legislation was originally passed. Congress should make it clear that DOD can no longer play games to avoid its legislative mandate by passing a clarifying amendment to the Small Business Act.

In a surprising development on August 12, SBA issued a rule, without going through notice and comment proceedings, that would allow procuring agencies to decide whether or not they would refer non-responsibility determinations on under $10,000.00 contracts to the SBA for Certificate of Competency purposes./14 In an apparent attempt to sidestep the requirements of the Regulatory Flexibility Act, SBA claimed that the rule had no impact on small business. This is utterly preposterous. Perhaps the most important impact of the COC program is not the COC's actually awarded, but the fact that it deters contracting officers from issuing baseless non-responsibility determinations. They know that if they issue a baseless determination, it will be reversed by the SBA. As you know, Public Law 95-507 reserves under $10,000.00 contracts for small business concerns where there are two or more responsible small business bidders. The result of this rulemaking brainstorm by the supposed protector of small business will likely be that contracting officers will steer such contracts to large business concerns on grounds that there are not two responsible small business bidders. We believe that the SBA owes the Committee some answers on this curious rulemaking effort that both substantively and procedurally frustrates its legislative mandate.

2. Congress should reaffirm the requirement that contracting officials obtain maximum practicable competition rather than the "effective competition" contemplated by the proposed Federal Procurement System.

Under present law, contracting officials are required to obtain maximum

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14/ 47 Fed. Reg. 34972 (1982).

practicable competition. They are also required, whenever possible, to utilize formal advertising in awarding contracts. Under formally advertised contracts, award is made to the lowest responsible and responsive bidder.

In the proposed Federal Procurement System recently presented to Congress by the Office of Federal Procurement Policy, only "effective competition" would be required and the preference for formal advertising would be eliminated. The rationale for these changes is that the present statutory requirements are routinely ignored and should be modified to reflect current practices.

Allowing less than maximum practicable competition and permitting the use of negotiation in lieu of formal advertising on a routine basis would permit procuring officials to award to other than the low bidder based upon subjective factors. In light of the billions of dollars already wasted by DOD annually as a result of their noncompetitive procurement practices, NTMA submits that the present requirements of maximum practicable competition and preference for formal advertising should be strictly enforced rather than weakened to provide a bootstrap justification for shoddy procurement practices.

3. Enact a clarifying amendment to the Small Business Act making it clear that procurement rulemaking is subject to the Regulatory Flexibility Act.

Despite the massive impact of procurement rules on small business concerns, the contracting agencies do not comply with the procedures set forth in the small business Regulatory Flexibility Act. The act requires agencies to use special techniques to assure the participation of small business in the rulemaking process, such as: (1)

publication of notice in publications read by small entities, and (2) a direct notification of effected parties. At present, DOD not only does not comply with the Regulatory Flexibility Act, but does not even publish notice of its rulemaking efforts in the Federal Register.

The Regulatory Flexibility Act also requires that notice of proposed rulemaking contain an initial regulatory flexibility analysis which sets forth:

- The reasons for the proposed rule;
- Its objectives and legal basis;
- An estimate of the number and type of affected small businesses;
- A statement of anticipated compliance requirements;
- Identification of any Federal rules which it duplicates, overlays or conflicts with; and
- A description of significant alternatives which accomplish the stated objectives and minimize the economic impact on small businesses.

Such procedural safeguards are badly needed, especially at DOD, and Congress should take the steps necessary to make sure that they are implemented.

4. Amend the Equal Access to Justice Act to allow small businesses to recover attorney's fees for successful GAO bid protests.

Noncompetitive procurement practices are often challenged by small business concerns in the form of GAO bid protests. The protestants are performing a public service because noncompetitive practices generally result in unnecessary Government expenditures.

As a result of apparent legislative oversight, successful protestors may not be able to recover their attorney's fees under the Equal Access to Justice Act. Attorney's fees under the Equal Access to Justice Act are only recoverable where a small firm is successful in court litigation or administrative litigation subject to the Administrative Procedure Act. Bid protests fall into neither category. In light of the public service performed by successful protestants, they too should be allowed to recover their attorney's fees and the Equal Access to Justice Act should be so amended.

As previously discussed, it would also be desirable to give GAO the authority to compel timely agency responses and to enjoin awards.

III. Conclusion.

In summary, NTMA is disturbed by current procurement practices that make it impossible for our membership and other small businesses to effectively compete for Government contracts. We believe that the time has come for meaningful reform in the direction proposed by Senator Specter.

We are not asking for a hand-out, but only a fair chance for our small business membership to serve our country's defense needs by competing for contracts which in most cases, they can perform more economically than the incumbant sole-source contractors.

This concludes our prepared statement. If you have any questions, we would be happy to address them.

Senator **Hayakawa**. We shall next hear from Mr. Leo Dondanville, Hanson Engineers, Inc., of Springfield, Ill.

STATEMENT OF LEO J. DONDANVILLE, PRESIDENT, HANSON ENGINEERS, INC., SPRINGFIELD, ILL., REPRESENTING THE AMERICAN CONSULTING ENGINEERS COUNCIL

Mr. **Dondanville**. Mr. Chairman, Senator Dixon, Hanson Engineers is a member firm of the American Consulting Engineers Council. In that capacity I am representing that organization this morning.

Our firm has approximately 65 employees, and our split of work is approximately 50 percent industrial and 50 percent Government at all levels.

As a representative of more than 120,000 personnel within the American Consulting Engineers Council's 3,800 firms, the vast majority of which are small businesses, ACEC appreciates this opportunity to testify on S. 2466.

We appreciate the committee's continuing initiatives on behalf of small business over the years, particularly your efforts this year in passage of the Prompt Payments Act of 1982, and S. 1947 which extends the minimum time period for solicitation of all Federal procurement contracts.

We support the major provisions of S. 2446 as a very much needed remedy in the area of Government contracts. The extension of the bid solicitation time period allows us to properly respond to the requests for services, line up subconsultants, and improve the quality of our responses, which in the long run will improve the quality of design services procured.

Similarly, the breakdown of large procurements is helpful to our group inasmuch as we are truly mostly small businesses.

The requirement to provide laws and regulations to firms contracting with the Government is again a much-needed provision. Many small businesses are disinterested in Federal work because of perceived complexities and ambiguities in the Federal laws and regulations. They do not have inhouse legal services, and, frankly, they are intimidated by the volume of boilerplate and paperwork.

Finally and very importantly, we understand the committee's motivation in requiring special justification for sole-source procurements. We also urge the committee to remember that the absence of competitive bidding does not necessarily imply sole-source procurement.

In the architect-engineer selection process, Public Law 92-582, the Brooks Act, has for over 12 years prescribed a system of competitive selection where price is very spiritedly negotiated by Federal administrators following selection based upon technical qualifications.

Other major provisions of the Small Business Procurement Act, which we would like to see addressed are the revision of the standard classification codes for business and industry sectors, particularly the Standard Industrial Code. We are uncomfortable with the Federal Procurement Data Service grouping architect-engineer services in this classification with services performed by nonarchitectural engineer contractors, such as Rockwell, Raytheon, Texas

Instruments, and that this classification includes such services as design work associated with nuclear aircraft carriers and submarines. We believe that if the SIC were narrower and more specific, these errors could be reduced.

In addition, consulting engineer services are included with services performed for the Federal Government by State and local government and not-for-profit institutions.

We believe that the standard industrial classification system needs attention, and we are particularly concerned that OMB has recommended postponing SIC system review and revision until 1987.

Finally, we urge the committee to actively explore the favorable impacts of contracting out for small businesses of all types. We recognize that the Senate Committee on Governmental Affairs has this jurisdiction, but small business engineering firms have long been concerned with the competition from inhouse Government design staffs, particularly the Corps of Engineers and the Bureau of Reclamation.

We believe it is time to pursue a number of approaches to making contracting out essentially the law of the land. Two such approaches we favor are Senate Joint Resolution 93, authored by you, Senator, and S. 1903 introduced by Senator Bentsen requiring a study of Federal government activities which can be performed more efficiently by small business.

We recognize that the jurisdiction on these matters must be shared and that there are sometimes conflicting interests within the Government and the private sector. However, the first casualty of greater inhouse performance is small business. We urge that the committee take action on this important issue.

Thank you, Mr. Chairman. That concludes my statement.

If you or other members have questions, I would be pleased to answer them. Thank you.

Senator HAYAKAWA. Thank you, Mr. Dondanville.

[The prepared statement of Mr. Dondanville follows:]

TESTIMONY OF LEO J. DONDANVILLE, PRESIDENT, HANSON ENGINEERS, INC., SPRINGFIELD, ILL., ON BEHALF OF THE AMERICAN CONSULTING ENGINEERS COUNCIL

Testimony of Leo J. Dondanville

Mr. Chairman and members of the Committee, my name is Leo Dondanville and I am President of Hanson Engineers, Inc., in Springfield, Illinois, a member firm of the American Consulting Engineers Council (ACEC). With me today is William J. Birkhofer, Director of Governmental Affairs of ACEC. Hanson Engineers has a staff of 65 employees and provides structural and foundation engineering services for bridges, buildings, earth dams and levees, as well as other engineering services. Approximately half our work is for industrial clients. The remaining 50 percent is done for the federal government directly or indirectly through federal assistance programs.

I appreciate this opportunity to represent the American Consulting Engineers Council in testifying on S. 2446 and other small business issues.

As a nationwide federation of over 3,800 independent engineering firms, ACEC represents more than 110,000 professional, technical and support persons. These firms range from sole proprietorships to multi-branch corporations. However, a very large majority are small businesses. Fields of practice include civil, electrical, mechanical, structural and geotechnical engineering, with projects ranging from acoustics to water pollution abatement.

As a representative of so many small firms, ACEC appreciates this Committee's continuing initiatives in establishing a healthy small business environment. Since 36 percent of the services consulting engineers perform over-all are for the federal government, directly or indirectly, ACEC particularly commends your efforts to pass the Prompt Payments Act of 1982 during this session of Congress.

ACEC also commends this Committee's introduction of S. 1947 (Section IV of S. 2446) amending Section 8(e) of the Small Business Act. This bill would extend the minimum time period for publication of and bidding on all federal contracts, thereby enhancing opportunities for small businesses to participate in the federal procurement process. ACEC strongly supports an extended time period and federal uniform contract advertising policy to assist small business federal contracting.

Major Provisions Of S. 2446

In our judgment, S. 2446 is a much-needed remedy for many longstanding problems facing small business in the procurement process. Notwithstanding the efforts of the Administration to develop and implement a uniform procurement system, the particular problems of small and small and disadvantaged business require special attention.

First, lengthening the response time in all solicitations is of particular benefit to small architectural and engineering firms. A great majority of ACEC member firms doing government work are located some distance from offices of federal agencies and the flow of information can be quite slow. Even those who subscribe to and monitor the Commerce Business Daily find that there is barely time to note the solicitation, contact the designated contracting or technical representative for additional information, line up other subconsultants and develop and submit a proposal within the two-week period typically provided for responses. Providing our firms up to 45 days to respond should lead to significant improvements in the quality of responses and thereby lead to improved quality in the design services procured.

The bill's requirement to break down large procurements will also serve to significantly broaden opportunities for small business architects and engineers, but perhaps in a sense not anticipated by the sponsors.

As the Small Business Administration (SBA) will relate, the architect-engineer profession is one of some 51 service and construction industries designated as "procurement sensitive"; i.e., industries particularly sensitive to government procurement needs. As a practical matter, what this means is that our profession bears a disproportionate share of systemwide small business utilization objectives in agencies such as the Department of Defense. In other words, a higher level of documented small business utilization in the architect-engineer field facilitates "agency procurement needs" by allowing contracting authorities to avoid significant small business utilization in other areas where large procurements are more convenient or desirable to agency procurement personnel. A universal requirement to break large procurements into smaller components will thus broaden small business utilization in other industry sectors and lessen the burden on the architect-engineer profession.

The bill's requirement that interested firms be provided with copies of all pertinent laws and regulations with which they must comply in performing the contract will not only save time, money and confusion, but should actually encourage more small business participation. I need not tell this Committee that many small businesses, including architect-engineer firms, are disinterested in federal work because of perceived complexities and ambiguities in federal laws and regulations. Many others, who typically do not have in-house legal resources, are intimidated by the volume of "boilerplate", most of which is written in "legalese". On a related note, new authority to allow SBA to assist small businesses in resolving minor contract disputes should be very helpful as well.

Finally, we understand the motivation of the sponsors of S. 2446 in requiring special justification for sole-source procurements or instances in which procurements are restricted to certain geographic areas. We would only urge the Committee to remember that the absence of "competitive bidding" does not necessarily infer "sole source procurement". For example, architect-engineer selection procedures, outlined in Public Law 92-582 (40 U.S.C. 471, et seq.), prescribe a system of "competitive selection" in which price is negotiated following selection based on technical qualifications.

We would also suggest that, from a small business perspective, there are trade-offs with respect to geographic procurement limitations. For example, limiting responses to solicitations for architect-engineer services to a given area or region may preclude a major firm outside the area from participation, thereby ensuring greater opportunities for small A-E firms adjacent to the proposed project to win the job.

Other Major Small Business Procurement Issues

There are other pressing areas of concern relating to small business which we would like to raise at this point for the Committee's attention. Some of these issues will undoubtedly have to be addressed in greater depth in the 98th Congress, and some can be addressed at least partly by SBA, but all are critically important to small and small and disadvantaged business.

First, we believe that the federal framework for classifying business and industry sectors needs considerable revamping to accurately portray the nature of small business in each sector and to properly measure the extent to which small businesses are utilized in the procurement process. Since the foundation for size standards development and the basis for small business utilization statistics is the Standard Industrial Classification (SIC) system, SICs must be narrow and specific rather than broad and general, and the range of product/service codes grouped under each must be similarly narrow and specific. For example, SIC 8911, which presently covers engineering, architectural and surveying services, is far too broad to cover the wide range of construction and non-construction-related services A-E firms typically provide. It may be desirable to delineate construction-related A-E services under Major SIC Group 15 or 16 (which include other construction activities) and account for other types of A-E services in Major Group 89. It may also be possible to differentiate within the major groups by employing five- or even six-digit SICs. In any event, we see it as being within SBA's mission to work actively within the Interagency SIC Committee to promote greater accuracy in using the SIC system in order to tailor size standards to "real world" industry conditions.

The same could be said for the operation of the Federal Procurement Data System, whose small business utilization statistics for the A-E profession are highly misleading and inaccurate, primarily due to the breadth of services typed as "architect-engineer" and the range of contractors considered to be "architect-engineers". For example, FPDS statistics, which are cited by SBA and other procuring agencies, supposedly reflect a relatively small percentage of small business utilization. Yet, the FPDS data includes "A-E services" performed by non-A-E contractors such as Rockwell International, Raytheon, Sperry and Texas Instruments, and include such services as design associated with nuclear-powered aircraft carriers and submarines Needless to say, such companies are not typically considered to be independent, professional design practitioners, nor are such services normally completed by independent architects of consulting engineers.

Significantly, these statistics also show significant "architect-engineer" work performed under "status of forces agreements" by foreign governments and by state and local government agencies and not-for-profit institutions.

Finally, the FPDS statistics typically measure small business utilization not on the basis of the "number of projects" but on "dollar volume", which skews the statistics even further. To our knowledge, the FPDS system does not record volume of work performed by small businesses under subcontract nor does it specifically delineate contract awards to minority- and women-owned businesses.

Again, we believe these "building blocks" of the small business procurement system need attention and we are particularly concerned that OMB has recommended postponing review and revision of the SIC system until 1987.

Another area of concern to ACEC is SBA's effectiveness in assisting small and disadvantaged firms' development through federal procurement opportunities. ACEC believes that the SBA 8(a) program is generally designed for the procurement of tangible goods and services for which there is a defined scope of work in advance; i.e., construction contracts. We feel that, historically, minority and women architects and engineers have not significantly benefitted from the program.

There appear to be no data available indicating potential concentrations of specific types of services provided by minority- and women-owned businesses. ACEC believes that this data would be valuable to SBA in determining which federal contracts should be set aside for small and disadvantaged firms. By first making this determination, and then matching federal contract opportunities to small and disadvantaged firms' capabilities, SBA would assist those businesses to develop by providing additional experience relating to the specific business area and increasing their potential capital development. Instead, the federal government sets aside contracts which they *presume* to be within the capabilities of small and disadvantaged firms.

ACEC favors a preferential federal assistance program for small and disadvantaged firms. By establishing a program of goals and set-asides specifically targeted for socially and economically disadvantaged business concerns through direct federal procurement, procurement under grants and subcontracting, SBA could establish a two-tiered system to assist both small and disadvantaged and small business.

It is important that businesses be capable of competing for procurement contracts, both in the 8(a) program and in the open marketplace. By establishing rigorous certification procedures to eliminate all but bona fide socially and economically disadvantaged firms from participation in the preferential programs, SBA would establish a more equitable arena for small and disadvantaged firms to bid on contract proposals. The establishment of criteria for both entry and graduation of firms to and from programs designed to assist developing minority- and women-owned firms could more satisfactorily ease firms from the preferential small and disadvantaged programs into the small business programs and, ultimately, into the open marketplace.

The 8(a) program is the only legislative authority to provide business opportunities for socially and economically disadvantaged firms. Therefore, ACEC supports legislative enactment of a preference program for utilization of minority- and women-owned firms.

ACEC believes that all programs for small business assistance should be administered by a single agency. The Small Business Act, as amended, empowers the Small Business Administration to assist small business. The operation of the Minority Business Development Agency in the Commerce Department is not only unnecessary, but could serve to diffuse the responsibility of the Small Business Administration in assisting small and small and disadvantaged firms. The current jurisdictional split of programs to aid women-owned businesses is a key example of this diffusion.

Finally, and perhaps most importantly, we urge the Committee to actively explore the favorable impacts of "contracting out" on small businesses of all types, though we recognize that the Committee on Governmental Affairs has jurisdiction over this matter.

As Senator Specter and others have noted, the federal government has adopted a policy favoring reliance on the private sector, as opposed to in-house government activities, for needed goods and services.

Regretably, however, this policy, embodied in OMB Circular A-76, has not been consistently or fully implemented.

Small engineering firms have long been concerned with the "contracting out" problem, particularly in the context of competition from in-house design staffs of the U.S. Army Corps of Engineers, the Bureau of Reclamation and other federal agencies. For example, in the Corps' civil works activities, approximately 75 percent of all planning and design work is completed in-house. The Bureau of Reclamation has consistently utilized in-house engineers to complete planning and design of dam projects, notwithstanding the fact that U.S. consulting engineers have been involved in sophisticated dam designs throughout the world.

In the current environment, examples of avoidance of "contracting out" continue to abound. Late last year, the Council was involved in a protracted effort to stave off an Environmental Protection Agency proposal to involve the Corps of Engineers in planning and design activities associated with its $1.6 billion Superfund hazardous waste clean-up program. On an even more current note, we recently learned that the Bureau of Reclamation is apparently investigating the possibility of developing non-federal financing to fund planning and development of hydropower development in Idaho, Utah, Montana, Wyoming and California by Bureau of Reclamation staff.

On top of all this, there have been a number of recent efforts in Congress to limit "contracting out", including a six-month moratorium which begins October 1, and provisions placing in statute the A-76 exemptions to "contracting out", which have been incorporated in the military pay bill (H.R. 6317), scheduled for action in the House next week.

Finally, OMB Circular A-76 is inadequate in many respects:

- It is difficult if not impossible to develop cost comparison standards that will fully and fairly equate the operations of a government agency with those of a small business. Many comparison items are understated by the government, others are not included and others (such as profit) simply have no equivalent and thus are not stated.
- Even if an adequate cost comparison methodology could be developed, the process by which the comparison is performed is highly suspect. The government is not only charged with developing the methodology but also applying it, without any involvement or participation by private-sector interests.
- Current A-76 cost comparison guidelines automatically "handicap" the private sector by allowing that "new starts" can be undertaken by government unless a ten-percent cost differential is demonstrated (again through government-conducted cost comparison).
- There are a number of exceptions to the A-76 requirements which government agencies can and do use

to "protect" certain activities from contracting out. One of these is "national defense", which understandably can and should be used to exempt direct combat and security-related activities, but should not be used to protect a planning and design role for the U.S. Army Corps of Engineers in civil works activities.

We believe that there are a number of approaches to making "contracting out" the "law of the land". Two such approaches we have studied and do favor are Senate Joint Resolution 93, authored by Senator Hayakawa, which affirms in law the basic policy of the federal government to rely on private enterprise to provide needed goods and services; and S. 1903, introduced by Senator Bentsen, to require a study of activities now performed by the federal government to determine which could be performed more efficiently by small business and to transfer those activities to the private sector.

While we again recognize that jurisdiction over this issue must be shared, we believe that the first casualty of greater in-house performance is small business and we urge the Committee to take some action on this important issue.

Mr. Chairman, this concludes my statement and I would be pleased to answer any questions you or members of this Committee might have.

Thank you.

Senator DIXON. Mr. Chairman, unfortunately, I have another committee meeting presently in session which I must attend. I want to thank these very excellent witnesses for their important contribution to the testimony on this particular bill.

Senator HAYAKAWA. Thank you, Senator.

This illustrates a fundamental point about all of us in the Senate. On a good day we only have to be in two places at the same time; on a bad day we have to be in three or four. For him, it is a good day.

Senator Dixon did have some questions for Mr. Dondanville. I will ask them of you in a few minutes. I have some other questions first.

In your testimony, Dr. Hess, did you mention the University of Missouri?

Dr. HESS. Yes.

Senator HAYAKAWA. You said a testing job was given to the University of Missouri laboratory which could have been done by private industry and there was no reason why it should have been given to a nonprofit organization?

Dr. HESS. Just this past Monday at our request a debriefing was held to explain the rationale for the award, but the basic question of why should they be competing against us remains.

Senator HAYAKAWA. I was curious about that because I was a university president before I reformed and became a politician. I was curious about this. How does the University of Missouri or any other university get into this business of direct competition with a private firm such as your own?

Dr. HESS. I am not sure.

Senator HAYAKAWA. Why do they do this?

Dr. HESS. There seems to be a gradual movement by many universities away from the public service role. Perhaps it is the tightening of budgets of nonprofits at this particular time that draws them in that direction. There is a lot of high-sounding talk using the term "University-Industry-Government" cooperation, in which universities actually are being encouraged to make their research more applicable and more down to earth. Such emphasis encourages them to cross the line that separates their public service role—fundamental research in the public interest—from the commercial activities which we feel small, for-profit businesses should be performing.

Senator HAYAKAWA. There is no particular way it can be refereed, is there?

Dr. HESS. When we go to a procurement officer for a debriefing, he tells us that he would be violating regulations if he did not compare the university's bid directly with ours on a dollar-for-dollar basis. Whether or not it was appropriate for them to bid, the fact that we are recycling tax dollars to the Federal Government in the process of working for them cannot be taken into account.

Something from the higher level of setting policy has to be done. We cannot come down on procurement officers for doing their jobs as defined to them.

Senator HAYAKAWA. Would this type of this job do anything educationally for the students of the University of Missouri?

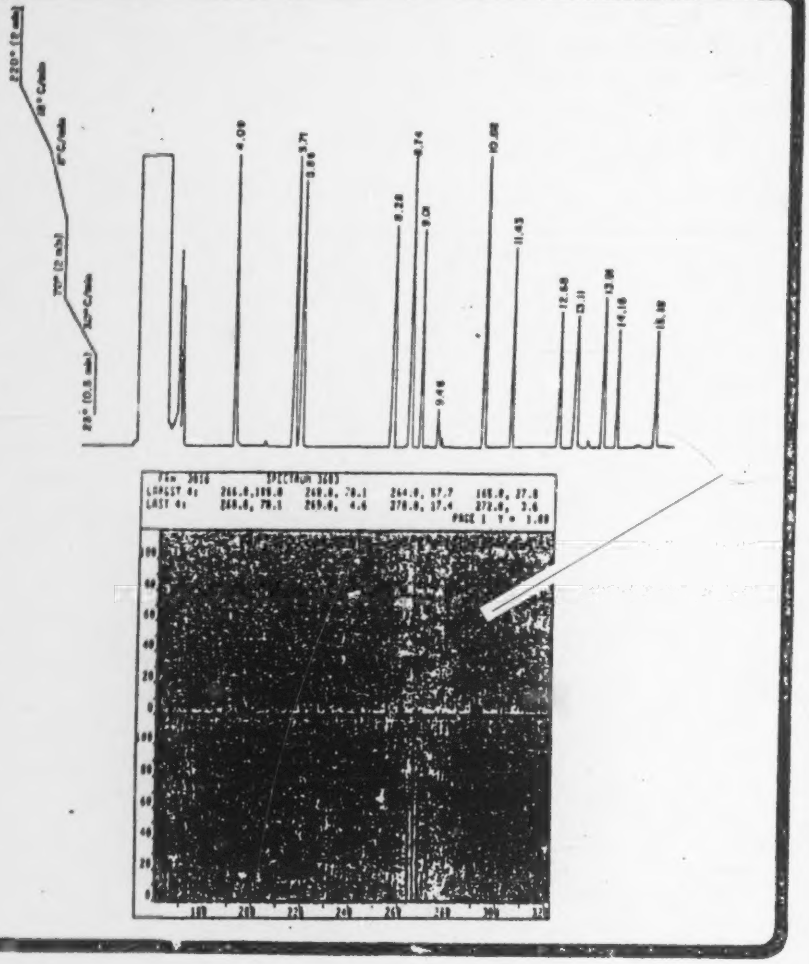
Dr. **Hess**. If testing hundreds and hundreds of rat feces samples for pathogenic organisms in behalf of the National Cancer Institute to be sure that their laboratory animals remain healthy during tests has an educational or research function, I do not know what it is.

Senator **Hayakawa**. I don't know, either, but then I am not a cancer expert.

Dr. **Hess**. I can show you—and I know we do not have time for it today—example after example of universities and nonprofits that are performing strictly repetitive analytical work. They are writing reports that look like my commercial reports. They have no research or public service role whatsoever. Attached is the promotional literature used by one university in a purely commercial activity.

[The material follows:]

ANALYTICAL SERVICES LABORATORY



Michigan Technological University's Analytical Services Laboratory supports University research in chemistry and related sciences, conducts research in analytical methods development and instrumentation, provides service to community organizations, and undertakes contract analyses. Michigan Tech's research is aimed towards the development of new analytical methods that will yield improved efficiency and accuracy as well as lower limits of detection. The laboratory provides quality analytical data to all clients and maintains an academic function in teaching and research.

Hazardous Waste Analysis

The analytical lab follows the sampling and analysis procedures of both the Resource Conservation and Recovery Act (RCRA) and the U.S. Environmental Protection Agency (EPA) "priority pollutant" protocol. Using RCRA procedures, samples are analyzed for such toxic compounds as endrin, lindane, methoxychlor, toxaphene, 2,4-D and 2,4,5-TP, and also for the elements arsenic, barium, cadmium, lead, mercury, selenium, and silver. EPA procedures used by the lab include methods for the analysis of volatile or purgeable organic compounds, extractable organics, cyanides, metals, phenols, and pesticides. The lab divides EPA "priority pollutants" into three groups: bases/neutrals, acids, and pesticides. Components of each fraction are then determined. Additional volatile organic priority pollutants are analyzed by either the Bellar-Lichtenberg volatile organic analysis (VOA) method or by direct aqueous analysis.

Water Analysis

The lab is equipped to perform several types of analyses on water samples. Analyses commonly performed by Standard Methods are chemical oxygen demand (COD), biological oxygen demand (BOD), and total organic carbon (TOC), as well as analyses of anions. Metals are analyzed by atomic absorption spectrophotometry using a Perkin-Elmer 305B equipped with an HGA 2100 graphite furnace. Most metallic elements can be determined with this instrument, and detection limits up to one thousand times better than conventional flame atomic absorption are obtained.

Exhaust Emission Analysis

The analytical lab solves operational as well as research problems. Currently, the lab supports the biology and mechanical engineering departments in research concerning the control and measurement of diesel engine exhaust emissions. The analytical lab analyzes the exhaust for inorganics such as sulfates and nitrates by taking filter samples from sampling probes in diesel exhaust. The analysis of the soluble organic constituents is more involved, requiring gas and liquid chromatography as well as combined gas chromatograph and mass spectrometer (GC/MS).

Analytical Quality Control

Michigan Technological University's lab offers its analytical services to industry, government agencies, and businesses who need precise, accurate analyses with state-of-the-art instruments. In most cases, data are available to the client two weeks after receipt of samples. The lab adheres to the EPA's quality assurance requirements. It also follows additional requirements established internally in accordance with quality assurance and quality control standards.*

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*The quality assurance documents are available upon request.

Michigan Technological University
Analytical Services Laboratory
Price List*

ATOMIC ABSORPTION (per metal)

	Single Sample	2-5 Same Metal**
Flame	20	10
Graphite Furnace	30	15
Mercury — cold vapor	40	25
Hydride	45	25
Sample Preparation		
a) Solid	5	5
b) Biological (digestion)	12	8
c) Preconcentration	10	10

CHROMATOGRAPHY

	Single Sample	2-5 (Similar Compositions)**
Organics (FID)	90	65
Pesticides/Organics (ECD)	120	75
Purge and Trap (FID)	110	75
Gas Chromatography Development	60/hour	–
HP Liquid Chromatography		
Monomeric Organics	100	80
HPLC Development	75/hour	–
Inorganic Anions by Ion Chromatography	15	10
IC Development	50/hour	–

MASS SPECTROMETRY

	Single Sample	2-5**
	80	60
Organics by Direct Probe		
Gas Chromatography-Mass Spectrometry		
1. Confirmation of Structure		
a) Known compound (library search)	90	65
b) Each additional search	25	20
c) New compound (manual)	120	90
d) Each additional unknown	40	40
2. Structure Elucidation	200	175
a) Each additional unknown	50	50
GC/MS Development	80/hour	–

EPA METHODS

		Single Sample	2-5*
601	Purgeable Halocarbons (29)	200	175
602	Purgeable Aromatics (7)	110	75
603	Acrylonitrile/Acrolein	80	70
604	Phenols (11)		
	a) FID	150	120
	b) ECD	180	150
605	Benzidines (2)	90	75
606	Phthalate Esters (6)	125	100
607	Nitrosamines (3)	125	100
608	Pesticides and PCB's (25)	160	130
609	Nitroaromatics and Isophorone (4)	100	85
610	PNA's (16)	200	175
611	Haloethers (5)	100	80
612	Chlorinated Hydrocarbons (9)	150	120
613	2,3,7,8 TCDD	300	250
624	Purgeables — GC/MS (30)	200	180
625	a) Base/Neutrals (47)	200	185
	b) Phenols (11)	160	140
	c) Pesticides and PCB's	200	185
	d) A,B,C and 624	600	550

RCRA — EP TOXICITY

	Single Sample	2-5**
Extraction — leach	75	50
Metals	255	150
Pesticides and Herbicides	150	120

*Prices subject to change without notice due to increasing costs of supplies.

**Six or more samples negotiated.

Information on procedures not listed available on request.

NOTE: MTU requires a memorandum of understanding or your purchase order in advance of service. Exceptions to this regulation are made for emergencies only.

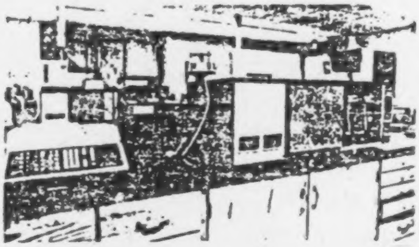
Specialized Techniques and Equipment

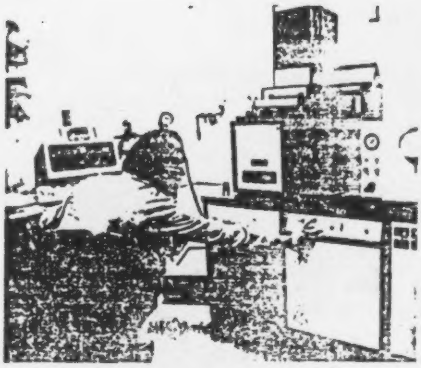
Liquid Chromatography: This technique yields high accuracy for thermally unstable or high molecular weight compounds. A chromatographic separation is achieved with the aid of a liquid mobile phase and analytical grade columns; ultraviolet and fluorescence detection are both available. Microprocessor-controlled automatic injection and fraction collection permit unattended operation for efficient sample throughput and/or semi-preparative scale use.

Hewlett-Packard 1084B Liquid Chromatograph

Large-scale preparative purification and collection can also be carried out after the analytical parameters are established.

Waters 500 Preparative Liquid Chromatograph





Gas Chromatography: This method is designed for the rapid separation of volatile compounds based on their differential distribution between two phases. The detectors available for this process include thermal conductivity, flame ionization, and electron capture. Ultra-high resolution capillary column and conventional packed column technologies are available.

Hewlett-Packard 5840 Gas Chromatograph

Hewlett-Packard 5880 Gas Chromatograph

GC/MS: This technique couples the separation power of gas chromatography with the high performance compound identification ability of mass spectrometry. Complete identification of components present at nanogram levels in complex mixtures is possible. GC/MS data can be supplied in hard copy form as well as 8-track magnetic tape in EPA format.

Hewlett-Packard 5985B

Ion Chromatography: Ion chromatography offers rapid routine analyses of many anions present at very low concentrations. This analysis uses an ion-exchange liquid chromatograph coupled to a high sensitivity conductometric detector.

Dionex Model 10 Ion Chromatograph

Versatility of Services:

The laboratory staff have analyzed sediments for mercury, air filters for diesel exhaust, coal for BTU content, contaminated soil samples for organic compounds, waste water and sludge for both organics and metals, constituents of extracts from Michigan oil shale, and products from wet oxidation reactors as well as synthetic anticancer agents.

Confidentiality

All information and data are kept in strict confidence. Data become the property of the client.

Contact: Dr. Wilson M. Gulick, Jr., Director
Analytical Services Laboratory
Michigan Technological University
Houghton, MI 49931

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Senator HAYAKAWA. Let me invite a quick answer to this question from each of you. Would each of you give me your view as to the single largest impediment for those small firms which would like to do business with the Federal Government?

Dr. HESS. I would have to say it is nonprofits.

Senator HAYAKAWA. Mr. Dondanville.

Mr. DONDANVILLE. I think for the very small firms it is intimidation by the contracting process itself, the auditing requirement.

Senator HAYAKAWA. Intimidation by the contracting process itself.

Mr. Hahn.

Mr. HAHN. I would say for our members who are not in the research community per se it is the process itself which is probably the biggest barrier.

Senator HAYAKAWA. Do you mean the process of getting the contract?

Mr. HAHN. Yes. You have to go through so many hoops. Although by law the Department of Defense and the branches are supposed to, whenever practical, competitively bid all of their procurements, the reverse is true. To get the Government to competitively bid a contract or to get to be able to participate, even just to participate in a competitive bid, is going through a maze. You have to go through a tremendous maze, and there are barriers in every corner.

Senator HAYAKAWA. I will ask the three of you again to respond as briefly as possible: What are your views on the current system for determining whether or not a business is small for the purpose of bidding on Federal contracts? How do they define "small"? We are going through a redefinition process.

Dr. HESS. I have some very strong feelings on that. The American Council of Independent Laboratories, whom I represent, has submitted statements. Looking at the whole process of size definition as it is proposed by SBA we see it skewed significantly by including a cottage industry in the computation that has shifted the maximum level down to very near my company's size. The point that I made before is that just about the time we are large enough and stable enough to go through the Government procurement hassle and tangle with it a little bit, we are eliminated.

The "cottage industry" to which I referred would not really be an entity with respect to Government procurement. Such very small laboratories would never even think about it. Therefore, I think the proposal formula is self-defeating and size definition needs to be looked at in some other way than it is at present.

Senator HAYAKAWA. Mr. Dondanville?

Mr. DONDANVILLE. The official position of the Consulting Engineers Council is to remove size standards for architectural engineerings firms. However, I would emphasize that most A-E firms, even with 150 or 250 people, really are lowly capitalized businesses where the stock is distributed among a number of people with small holdings and could be considered small business.

Senator HAYAKAWA. Mr. Hahn.

Mr. HAHN. As I mentioned earlier, our typical company is 15, 20, maybe 25 employees. Of the 14,000 companies in the industry, I think I could count on my fingers and toes those which are over 100 employees.

We do not have a position and, frankly, probably I would have to ask, but I do not think our members would care what you did on the size standards. I know it has been a can of worms and that we have tried a number of times to establish a standard.

I suspect our position would be that they would be irrelevant if you would just competitively bid Federal procurements. Why do you need this protection for small businesses in chopping off a tiny little piece of the pie and say, "We will reserve that" and then fight over the size standard? Why don't they just make it openly competitive? We will compete with anybody. We will compete with McDonnell-Douglas. We don't care.

Dr. HESS. I agree with that philosophy. I am not a strong protectionist.

I would like you to pay some attention to the recommendations made by the White House Conference on Small Business with respect to size standards, which suggested an A, B, C, D, classification type. We have been told by SBA and agencies that this is entirely too complicated to work. I disagree. There are situations in which a small business, under 15 employees perhaps, should be protected for a special purpose. That does not mean that if you have more than 15 employees, that you are all of a sudden invited to the Business Roundtable. The graduated approach has some very strong and positive elements which we uphold in our statement to the SBA on the issue.

Senator HAYAKAWA. As a small business contractor, do you think the arbitration panels provided for in S. 2446 would be of any use to you in settling disputes?

I invite any of you to comment.

Mr. DONDANVILLE. I think they definitely would because in any construction contract or engineering service contract dispute the technical items are such that if they go to court they are sometimes interpreted in different ways and legal expenses are very, very expensive.

Any internal negotiations system would be very helpful.

Senator HAYAKAWA. Thank you.

Dr. Hess.

Dr. HESS. We, as a small business, in writing contracts with non-Government clients always include an article which designates arbitration as the means of settling disputes for the very reason that small business cannot afford the high legal expenses. I am not quite sure what this provision does to "equal access to justice." That is one strength, after all, that small business now has. If one has a solid case, he can take the Government to court, win, and get paid for his legal expenses.

Senator HAYAKAWA. Mr. Hahn, do you want to comment on that?

Mr. HAHN. I would like to call on our counsel, Mr. Paul Seidman, who is with me who has some particular insight on that, having formerly been with SBA's Office of Advocacy and specializing in procurement.

Mr. SEIDMAN. The first thing to note is that there are two types of disputes which would be covered by the Specter bill. One is preaward disputes, in other words, disputes concerning who would get a particular contract, and also postaward disputes, which are basically claims, terminations for default, and so on.

As far as preaward disputes, most of those now are handled by GAO. Most small businesses do not go to the Federal courts because of the cost.

Giving this to arbitration panels at SBA, I really do not know whether it would accomplish anything. You have people in place already handling it with the expertise. If they were given the authority to compel timely responses from procuring agencies and to enjoin procurements pending their decision, protests might be of some value.

Right now representing small businesses at GAO, I find very often you win the battle and lose the war. The contract is already awarded by the time the protest is decided, so even if you win, you lose.

The second point concerning postaward disputes, in the Contract Disputes Act of 1978 it sets forth expedited procedures for claims of under $10,000 for using informal procedures. A decision would be issued on the claim within 120 days after a request for the expedited procedures was made.

A similar procedure is for claims of $50,000 and less, and a decision there, using informal procedures, would be rendered within 180 days after a business requested such a use of the accelerated procedures.

We believe that these procedures are adequate. We note, however, that in the Contract Disputes Act of 1978 there is a provision in there suggesting that the OFPP review the dollar thresholds periodically for inflation. They are given this authority for under $10,000 contracts, and, although there has been a good deal of inflation since 1978, the dollar threshold never has been adjusted. Perhaps OFPP could take a positive step to help small business by raising those dollar thresholds at this time.

The way I read the Contract Disputes Act, they do not have the authority to raise the threshold for the under $50,000 contracts but perhaps Congress should give that to them.

Senator HAYAKAWA. Thank you.

If there are further questions, I shall submit them in writing and ask for your written replies. We have other panels to hear this morning.

However, before breaking up this panel, I would like to submit to you, Mr. Dondanville, the specific question left for you by Senator Dixon.

Mr. Dondanville, you mentioned the SIC codes are unsatisfactory in the A-E industry. Could your association provide the committee with specific suggestions for SIC code modifications which we in turn could submit to SBA? I understand "SBA." [Laughter.]

If you wish to answer this question in writing, that is OK, or do you have a quick comment on it?

Mr. DONDANVILLE. I have a quick comment. First of all, the current code is, I believe, 8911.

Senator HAYAKAWA. Code of what?

Mr. DONDANVILLE. The SIC code.

Senator HAYAKAWA. What is SIC?

Mr. **Dondanville**. Standard industrial classifications.

Senator **Hayakawa**. In the A-E industry?

Mr. **Dondanville**. That is right. That is the classification under which small business Federal procurement data is accumulated and analyzed by many Government agencies.

Senator **Hayakawa**. All right.

Mr. **Dondanville**. At the current time this SIC 8911 classification includes architects, engineers, and surveyers, but also design services for such unrelated things as naval architecture and such.

We believe that the classification should be narrowed rather than broadened, be more specific to more clearly define—possibly have between the types of services currently grouped within the SIC 8911 category. There might be classifications added in the 1500 series, which could refer to design services for buildings, and in the 1600 series which could relate to construction-related design for highway and heavy construction. These would be our suggestions.

Senator **Hayakawa**. Thank you.

Mr. **Dondanville**. We can respond further in writing if you would like.

Senator **Hayakawa**. Fine. Thank you.

[Subsequent information was received and follows:]

ACEC File #700.01

american
consulting engineers
council

UNITED STATES MEMBER

1015 FIFTEENTH STREET, N.W., WASHINGTON, D.C. 20005-2670 ☐ (202) 347-7474
Telex 897445 AMCONENGRC WSH

November 4, 1982

The Honorable Lowell P. Weicker, Jr.
Chairman, Select Committee on Small Business
United States Senate
424 Russell Senate Office Building
Washington, D.C. 20510

Dear Senator Weicker:

During the Senate Small Business Committee hearing on the Small Business Procurement Reform Act of 1982 (S. 2446) on September 16, 1982, the Committee asked the American Consulting Engineers Council (ACEC) to provide specific suggestions for Standard Industrial Classification (SIC) modifications.

The Small Business Administration (SBA) is currently revising small business size standards for numerous industries, including consulting engineers. The foundation for size standards development and the basis for small business utilization statistics is the Standard Industrial Classification system, first established in 1939 and periodically revised to "better reflect statistically the existing industrial structure of the economy."

ACEC recognizes the SIC as one of the most important tools that has been developed to promote the comparability of statistics describing various facets of the economy of the nation. Developed initially for use within government for statistical purposes (including small business utilization information), the SIC is now widely used by state agencies, trade associations, private business and other organizations.

While ACEC supports the SIC as an important vehicle with which to collect, compile and analyze data relating to establishments, we question the

President RUSSELL L. SMITH, JR. Honolulu, Hawaii • *Senior Vice President* FU HUA CHEN Denver, Colorado
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methodology employed by SBA in using the current SIC to establish small business size standards.

The Small Business Administration initially announced the small business size standard revisions in March, 1980 (see Appendix A). Numerous public comment to the notice of size standard revisions resulted in SBA revising its methodological approach to size standards in May, 1982. SBA received more than 1,500 comments from public hearings and individual written correspondence encompassing 200 of the 726 SIC industries. Comments received regarding the initial announcement of the revisions resulted in SBA revising 548 of the proposed size standards. SBA is expected to issue its final size standard ruling in the future, following public hearings and additional review and analysis.

It is our view that careful analysis of the proposed rule-making and the comments submitted will demonstrate that the second proposal of size standard revisions reflected no appreciable improvement in the methodology by which SBA devises its size standards. While we commend SBA for its intentions to give smaller firms the benefit of SBA's limited resources, we strongly suggest that the out-dated data used to define industries affects the Small Business Administration's ability to define small businesses.

The 1972 SIC Manual and its 1977 Supplement, which are the foundation being used by SBA to identify industries for the purpose of assigning size standards, is out-dated. The Office of Federal Statistical Policy and Standards (OFSPS), which is responsible for the compilation and revision of the SIC Manual, proposed structural changes to the SIC 1972 Manual and the 1977 Supplement in the "Federal Register" on January 30, 1981:

> "The proposed structural changes included in this announcement are based largely on recommendations of the Interagency Technical Committee on Industrial Classification (TCIC). Business, Industry and Federal and State Agencies had submitted 242 proposals for change . . . . The TCIC evaluated all of these proposals for change and recommended approximately one-third for acceptance and inclusion in a revised SIC."

The 1982 SIC Manual incorporating the 269 industry changes affecting more than 25 percent of the industries defined in the SIC was not printed, due to Office of Management and Budget (OMB) budgetary constraints. In January, 1982, OMB announced delay of the previously scheduled 1982 SIC Manual until 1987. Consequently, the Small Business Administration is revising industry size standards based on statistics that are not only at least ten years old, but also, to a substantial extent, are based on industry definitions that have been determined by the OFSPS to be obsolete. ACEC questions OMB's cost-benefit rationale of delaying the SIC Manual revisions until 1987. We believe that the costs saved will be exponentially accrued by the small business owners whose firms are inaccurately defined in the revised size standards.

In addition, we believe that the Small Business Administration must modify the industry categories within the SIC to narrowly and specifically define industries. The SIC codes were designed to classify "industry" in the broad sense of all economic activity.

ACEC agrees with SBA's view that distribution of firms by size within each industry is a key element of industrial structure. However, we question SBA's assertion that the broad and general SIC industry categories help determine where size limits are set and question more seriously that the proposed size standard changes specifically reflect the structure of each individual industry and SBA's ability to concentrate its assistance heavily on smaller firms.

With this background, we would like very much to see the Committee undertake a thorough review of OMB's decision to delay revision of the SIC Manual, the efficacy of SBA's proposed changes in size standards based on the out-dated 1972 SIC codes and their broad and general applications and the economic impact that such changes would have on the affected industries.

Sincerely,

William J. Birkhofer
Director
Governmental Affairs

WJB:tr

SMALL BUSINESS ADMINISTRATION

13 CFR Part 121

Small Business Size Standards; Revision to Method of Establishing Size Standards and Definitions of Small Business

AGENCY: Small Business Administration.

ACTION: Advance Notice of Proposed Rulemaking.

SUMMARY: The Small Business Administration is proposing an amendment to its size standard regulations which affect eligibility for SBA programs. The revision is designed to update and improve the logic, methodology, and presentation of the size standard procedures. The proposed regulation will simplify SBA programs for the small business community, reduce administrative complexity, and increase the effectiveness of SBA programs by improved targeting of its resources.

DATE: Written comments must be submitted by May 9, 1980.

ADDRESS ALL COMMENTS TO:
Kaleel C. Skeirik, Chief, Size Standards Division, Small Business Administration, 1441 L Street, N.W., Room 500, Washington, DC 20416.

FOR FURTHER INFORMATION CONTACT:
Kaleel C. Skeirik, (202) 653-6373.

SUPPLEMENTAL INFORMATION:

Highlights of Proposed Regulations

1. Size standards are intended to enhance competition and promote entry.
2. Size standards are established by industry based on a consistent overall philosophy.
3. The data and methodology used to develop size standards are current and well documented.
4. Each designated industry size standard will be used for all SBA programs.
5. Only one measure of a firm's size is used.
6. The size standard regulations and procedures are simplified.

Philosophy of Size Standards

> The essence of the American system of private enterprise is free competition. . . . The preservation and expansion of such competition is basic not only to the economic well-being but to the security of this Nation. Such security and well-being cannot be realized unless the actual and potential capacity of small business is encouraged and developed. It is the declared policy of the Congress that the Government should aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns in order to preserve free competitive enterprise. . .
>
> Small Business Act, Section 2(a)

To implement this policy Congress established the Small Business Administration (SBA) and gave it the responsibility to administer a range of programs designed to achieve these goals. Eligibility for SBA programs requires that a firm be "small." Establishing "size standards," i.e., the precise specification of "small," is delegated to the Administrator of the SBA.[1]

SBA's proposed size standards rest upon two premises. The first is that what constitutes a "small" business is different in different industries; regardless of how one measures the size of a business, e.g., number of employees, dollar volume of receipts, there is large interindustry variation. Second, that the resources of the SBA, given to it by taxpayers through the Congress, should be used to assist small business in order to enhance the intensity of competition in the U.S. economy.

The legislative history of the Small Business Act demonstrates that size standards must be established in the context of the industrial structure of the U.S. economy. The national economy is made up of hundreds of different industries, each one possessing its own unique characteristics, history, and dynamics. For the purposes of simplicity each industry can be classified by its degree of "competition."

The use of the term "competition" is very important to understanding the policy role of size standards. There are at least three different ways in which the term competition is used. First, there is the notion of business rivalry, of individual firms competing for sales. Usually, this is what a businessman thinks of when he speaks of competition. In this sense, most businesses compete. A second sense in which competition is used is in Government procurement, viz., competitive bidding. In this instance, a number of firms bid for contracts, either in open competition (between firms both large and small) or under set-asides where only small firms may enter into the competitive bidding. Third, there is the professional economist's meaning of competition. For the economist, competition takes place for an industry as a whole, not for individual firms; an industry is competitive when no single firm, or group of firms, is able to exert any control over the price of their product. Thus, farming or the construction industry is competitive; the automobile manfacturing industry is not.

In setting size standards the economist's idea of competition is used. Each individual industry was, initially, placed into one of three broad categories of industry: "competitive," "concentrated," and "mixed." The group of concentrated industries is characterized by a highly unequal distribution of sales among the firms in the industry, e.g., the four largest firms accounting for more than half the industry's sales. Competitive industries display a more equal distribution of sales, and the average firm is relatively small when measured by annual sales or number of employees. The group of mixed industries is the residual, viz., those industries which did not meet the criteria of competitive or concentrated industries. The study which led to the development of the size standards found 317 competitive industries, 160 concentrated industries, and 249 mixed industries.[2]

Given this classification of industries, the question now becomes which firms in each industry (or group of industries) shall be made eligible for SBA programs. Because the Small Business Act precludes SBA assistance to firms which "are dominant" in their industries, establishing a size standard in concentrated industries is a straightforward task—simply identify and exclude these few firms which account for a disproportionately large share of the industry's sales. This could enhance competition by providing support to all firms, in these concentrated industries, except the dominant ones.[3]

In industries which currently exhibit an intense level of competition, does any justification for SBA intervention exist? Historically, SBA has accepted the idea that the smallest businesses, regardless of their industry, are worthy of support. This has been justified on the grounds that it is a positive social, economic, and political act to provide opportunity for entry into the business world. Individual initiatives toward entrepreneurship should be encouraged by the Federal Government and meeting this responsibility is part of the mission of SBA. In such competitive industries size standards should be set relatively low, so as to support entry and moderate growth. Because such industries are already competitive, SBA intervention will not necessarily enhance competition.

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[1] Size standards only define eligibility for SBA programs. SBA strongly urges that its resources and its experience be utilized in developing definitions of "small" business that are responsive to the statutory missions of other Federal agencies and which are accurate reflections of the realities of the small business sector.

[2] While these 726 industries do not constitute all U.S. industries, they do comprise the traditional clientele of the SBA.

[3] The SBA is neither equipped nor desirous of assisting firms whose size exceeds some absolute size, say, 2,500 employees. This is a minor adjustment to this proposition.

The SBA role in mixed industries requires high size standards be set so as to carry out its legislative mandate to enhance competition. By making available its programs to those firms whose very presence acts as a constraint on the anticompetitive behavior of larger firms, SBA can reinforce competition and offset the pressures to increase the degree of concentration in these industries. Some of the mixed industries are experiencing significant changes in their market structures and display increasing concentration. SBA's intervention in these industries will be designed to maintain competition.

It is the view of SBA that firms which meet size standards and are eligible for SBA programs be given prompt and effective assistance. Small business concerns should not become dependent on continuing assistance under the Small Business Act from the "cradle to the grave" but should plan for the day on which they can thrive without such assistance.

Data and Methodology

The process of transposing this philosophy to numerical size standards for individual industries is a complex one. The basic sources of data used in establishing size standards include: *the Standard Industrial Classification Manual,* which is used as a guide in defining industries; U.S. Bureau of the Census, *Concentration Ratios in Manufacturing,* and *Enterprise Statistics;* a special tabulation of the *1972 Enterprise Statistics* prepared for SBA by the U.S. Bureau of the Census; U.S. Department of Commerce, *U.S. Industrial Outlook* and *Survey of Current Business;* Internal Revenue Service, *Statistics of Income;* Dun and Bradstreet's *DMI Market Profile;* Economic Information Service's *Marketing Information;* SBA's own extensive files of articles and correspondence on individual industries and information provided by trade associations. From these data sources, several measures of each industry's structure are available. The factors examined for the purpose of setting size standards included: average firm size, the extent of industry dominance by large firms as described by the concentration ratio and the Herfindahl index, the number of firms, the distribution of sales and employees among the firms in the industry, and the nature of entry barriers. The development of size standards is not an exact quantitative procedure. No single measure or simple numerical device was used to establish an industry's size standard. The process can be described as an exercise of informed judgment based on the policy considerations described above, viz., setting high size standards in concentrated and mixed industries in order to include larger firms so as to sustain and enhance competition, while setting size standards low in competitive industries tend to assure the opportunities for entry and to protect the smallest business.[4]

A Single Size Standard

A single size standard is proposed for all SBA programs. This constitutes a step toward the simplification of Government. Currently, there are separate size standard eligibility criteria among SBA programs. This leads to confusion for small businesses needing assistance, complexity for SBA employees responsible for administering its programs, and severe criticism by those who have studied SBA's size standards. Moreover, moving to a single size standard will eliminate the anomalous situation where a particular business firm is defined as "small" and eligible for assistance through one SBA program and not "small" and hence ineligible for assistance through another program.

One Measure of Size

All proposed size standards are stated in terms of a firm's number of employees. This is an improvement over the current system which uses many different measures of a business' size.

SBA has found that when size standards are denominated in dollars, i.e., annual revenues, its ability to help the small business sector is undermined by inflation. Using employment, as opposed to dollar sales, will provide greater stability for SBA and its clients; will remove interindustry distortions generated by differential inflation rates; and reduce the need for SBA to make frequent revisions in the size standards merely to reflect price increases.

Implementation Plan

SBA appreciates the fact that in some industries, and for some programs, the proposed size standards constitute a major change in their business environment. To be most responsive to the requirements of the small business sector SBA is not proposing a schedule for the implementation of the proposed size standards. Rather we invite your comments on the merits of alternative implementation schemes. Included among issues under consideration are: should the implementation timetable be the same for all SBA programs; should industries where the size standard has been raised be treated the same as industries where the size standard has been lowered; should implementation be scheduled on an incremental basis or take effect at one time; what should be the total length of time before all new size standards are put into effect; should different industries be given different amounts of time to comply with the new size standards.

Future Study

SBA's proposed size standards should not be viewed as permanent but rather as an ongoing process. SBA must be responsive to the dynamic structural changes constantly occurring in the economy as well as the changing needs of the small business community. Furthermore, SBA must strive to improve the accuracy and timeliness of the data, the level of analytical sophistication, and the quality of judgment brought to bear on the problems of setting size standards. Among the areas for future study being considered by the SBA are: an analysis of trends and projections of the patterns of concentration in U.S. industries; a study of differential entry and growth requirements among industries and their implication for SBA.

Comments

The proposed size standards are a major departure from SBA's "business as usual" posture. We strongly believe that this proposal will strengthen both the small business community and the SBA. The designation of particular size standards in individual industries is of concern to SBA, and we invite comments from all affected parties. However, we hope that public attention is also paid to the logic, philosophy, and design of the size standards. For the ability of the SBA to carry out its statutory mission requires an accurate reading of the statute and its legislative history, a reasoned application of SBA's mandate to the myriad empirical complexities of the U.S. economy, judicious appreciation of the strengths and limitations of SBA's programs, and a strong commitment to the success of the small business community.

Regional Hearings

In view of the fact that the proposed size standards include significant changes and are comprehensive in scope, the SBA expects to conduct public regional hearings during the time the proposed revised regulations are published for public comment in the **Federal Register.**

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[4] A comprehensive technical discussion of the concepts, data, and methodology is contained in The Size Standards Study. To obtain a copy contact: Chief, Size Standards Division, Small Business Administration, 1441 L Street, N.W., Washington, D.C. 20416. (202) 653-6373.

Accordingly, pursuant to Section 3 and 5(b)(6) of the Small Business Act, as amended (15 U.S.C. 632, 634), it is proposed to amend Part 121 of Title 13 of the Code of Federal Regulations as follows:

(1) By redesignating § 121.3–2 as § 121.6.

(2) By redesignating § 121.3–4 as § 121.7.

(3) By redesignating § 121.3–5 as § 121.8.

(4) By redesignating § 121.3–6 as § 121.9.

(5) By deleting § 121.3, § 121.3–1, § 121.3–3, § 121.3–7, § 121.3–8, § 121.3–9, § 121.3–10 through § 121.3–16 and Schedules A through I.

(6) By adding § 121.1 through § 121.5, as set forth below.

(7) The Table of Contents for Part 121 reads as set forth below:

PART 121—SMALL BUSINESS SIZE STANDARDS

Sec.

Subpart A—Background

121.1 Purpose—Method of Establishing Size Standards.

Subpart B—Definition of Small Business

121.2 Standard Industrial Classifications and Employee Size Standards.
121.3 Application of Small Business Size Standards.
121.4 Definition of Small Business for Procurement Assistance Programs.
121.5 Definition of Small Business for the Sale of Government Property Sales.

Subpart C—Procedures

121.6 Definitions.
121.7 Size Determinations
121.8 Protest of Small Business Status.
121.9 Appeals.

Subpart A—Background

§ 121.1 Purpose and method of establishing size standards.

> The essence of the American system of private enterprise is free competition. . . . The preservation and expension of such competition is basic not only to the economic well-being but to the security of this Nation. Such security and well-being cannot be realized unless the actual and potential capacity of small business is encouraged and developed. It is the declared policy of the Congress that the Government should aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns in order to preserve free competitive enterprise. . . .
>
> Small Business Act, Section 2(a)

(a) To implement this policy Congress established the Small Business Administration (SBA) and gave it the responsibility to administer a range of programs designed to achieve these goals. Eligibility for SBA programs requires that a firm be "small." Establishing "size standards," i.e., the precise specification of "small," is delegated to the Administrator of the SBA.[1]

(b) SBA's size standards rest upon two premises. The first is that what constitutes a "small" business is different in different industries; regardless of how one measures the size of a business, e.g., number of employees, dollar volume of receipts, there is large interindustry variation. Second, that the resources of the SBA, given to it by taxpayers through the Congress, should be used to assist small business in order to enhance the intensity of competition in the U.S. economy.

(c) The legislative history of the Small Business Act demonstrates that size standards must be established in the context of the industrial structure of the U.S. economy. The national economy is made up of hundreds of different industries, each one possessing its own unique characteristics, history, and dynamics. For the purposes of simplicity each industry can be classified by its degree of "competition."

(d) The use of the term "competition" is very important to understanding the policy role of size standards. There are at least three different ways in which the term competition is used. First, there is the notion of business rivalry, of individual firms competing for sales. Usually, this is what a businessman thinks of when he speaks of competition. In this sense, most businesses compete. A scond sense in which competition is used is in Government procurement, viz., competitive bidding. In this instance, a number of firms bid for contracts either in open competition (between firms both large and small) or under set-asides where only small firms may enter into the competitive bidding. Third, there is the professional economist's meaning of competition. For the economist competition takes place for an industry as a whole, not for individual firms; an industry is competitive when no single firm or group of firms is able to exert any control over the price of their product. Thus, farming or the construction industry is competitive; the automobile manufacturing industry is not.

(e) In setting size standards the economist's idea of competition is used. Each individual industry was, initially, placed into one of three broad categories of industry: "competitive," "concentrated," and "mixed." The group of concentrated industries is characterized by a highly unequal distribution of sales among the firms in the industry, e.g., the four largest firms accounting for more than half the industry's sales. Competitive industries display a more equal distribution of sales and the average firm is relatively small when measured by annual sales or number of employees. The group of mixed industries is the residual, viz., those which did not meet the criteria of competitive or concentrated industries. The study which led to the development of the size standards found 317 competitive industries, 160 concentrated industries, and 249 mixed industries.[2]

(f) Given this classification of industries, the question now becomes which firms in each industry (or group of industries) shall be made eligible for SBA programs. Because the Small Business Act precludes SBA assistance to firms which "are dominant" in their industries, establishing a size standard on concentrated industries is a straightforward task—simply identify and exclude these few firms which account for a disproportionately large share of the industry's sales. This could enhance competition by providing support to all firms, in these concentrated industries, except the dominant ones.[3]

(g) In industries which currently exhibit an intense level of competition, does any justification for SBA intervention exist? Historically, SBA has accepted the idea that the smallest businesses, regardless of their industry, are worthy of support. This has been justified on the grounds that it is a positive social, economic, and political act to provide opportunity for entry into the business world. Individual initiatives toward entrepreneurship should be encouraged by the Federal Government and meeting this responsibility is part of the mission of SBA. In such competitive industries size standards should be set relatively low, so as to support entry and moderate growth. Because such industries, are already competitive SBA intervention will not necessarily enhance competition.

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[1] Size standards only define eligibility for SBA programs. SBA strongly urges that its resources and its experience be utilized in developing definitions of "small" business that are responsive to the statutory missions of other Federal agencies and which are accurate reflections of the realities of the small business sector.

[2] While these 726 industries do not constitute all U.S. industries, they do comprise the traditional clientele of the SBA.

[3] The SBA is neither equipped nor desirous of assisting firms whose size exceeds some absolute size, say, 2,500 employees. This is a minor adjustment to this proposition.

(h) The SBA role in mixed industries requires high size standards be set so as to carry out its legislative mandate to enhance competition. By making available its programs to those firms whose very presence acts as a constraint on the anticompetitive behavior of larger firms, SBA can reinforce competition and offset the pressures to increase the degree of concentration in these industries. Some of the mixed industries are experiencing significant changes in their market structures and display increasing concentration. SBA's intervention in these industries will be designed to maintain competition.

(i) The process of transposing this philosophy to numerical size standards for individual industries is a complex one. The basic sources of data used in establishing size standards include: *the Standard Industrial Classification Manual*, which is used as a guide in defining industries; U.S. Bureau of the Census, *Concentration Ratios in Manufacturing*, and *Enterprise Statistics;* a special tabulation of the *1972 Enterprise Statistics* prepared for SBA by the U.S. Bureau of the Census; U.S. Department of Commerce, *U.S. Industrial Outlook* and *Survey of Current Business;* Internal Revenue Service, *Statistics of Income;* Dun and Bradstreet's *DMI Market Profile;* Economic Information Service's *Marketing Information;* SBA's own extensive files of articles and correspondence on individual industries and information provided by trade associations.

(j) From these data sources several measures of each industry's structure are available. The factors examined for the purpose of setting size standards included: average firm size, the extent of industry dominance by large firms as described by the concentration ratio and the Herfindahl index, the number of firms, the distribution of sales and employees among the firms in the industry, and the nature of entry barriers. The development of size standards is not an exact quantitative procedure. No single measure or simple numerical device was used to establish an industry's size standard. The process can be described as an exercise of informed judgement based on the policy considerations described above, viz., setting high size standards in concentrated and mixed industries in order to include larger firms so as to sustain and enhance competition, while setting size standards low in competitive industries tends to assure the opportunities for entry and to protect the smallest businesses.

(k) It is the view of SBA that firms which meet size standards and are eligible for SBA programs be given prompt and effective assistance. Small business concerns should not become dependent on continuing assistance under the Small Business Act from the cradle to the grave but should plan for the day on which they can thrive without such assistance.

Subpart B—Definition of Small Business

§ 121.2 Standard industrial classifications and employee size standards.

The size standards for all the manufacturing and nonmanufacturing industries (except for agriculture) are on employment basis. The following size standards are to be used when determining the size status of applicants for all SBA assistance programs, *except sales of Government property.*

Sic	Description	Size of standards (No. of employees)[1]
Div. A	Agriculture (see size standards at end of section	
Div. B	Mining	
	Major Group 10—Metal Mining	
1011	Iron Ores	1,000
1021	Copper Ores	2,500
1031	Lead and Zinc Ores	2,500
1041	Gold Ores	250
1044	Silver Ores	250
1051	Bauxite and Other Aluminum Ores	250
1061	Ferroalloy Ores, Except Vanadium	250
1081	Metal Mining Services	250
1092	Mercury Ores	100
1094	Uranium-Radium-Vanadium Ores	500
1099	Metal Ores, Not Elsewhere Classified	250
	Major Group 11—Anthracite Mining	
1111	Anthracite	250
1112	Anthracite Mining Services	100
	Major Group 12—Bituminous Coal and Lignite Mining	
1211	Bituminous Coal and Lignite	250
1213	Bituminous Coal and Lignite Mining Services.	250
	Major Group 13—Oil and Gas Extraction	
1311	Crude Petroleum and Natural Gas	250
1321	Natural Gas Liquids	2,500
1381	Drilling Oil and Gas Wells	200
1382	Oil and Gas Field Exploration Services.	250
1389	Oil and Gas Field Services, Not Elsewhere Classified.	250
	Major Group 14—Mining and Quarrying of Non-Metallic Minerals, Except Fuels	
1411	Dimension Stone	100
1422	Crushed and Broken Limestone	100
1423	Crushed and Broken Granite	190
1429	Crushed and Broken Stone, Not Elsewhere Classified.	250
1442	Construction Sand and Gravel	100
1446	Industrial Sand	250
1452	Bentonite	100
1453	Fire Clay	100
1454	Fuller's Earth	500
1455	Kaolin and Ball Clay	500
1459	Clay, Ceramic, and Refractory Minerals, Not Elsewhere Classified.	200
1472	Barite	500
1473	Fluorspar	500
1474	Potash, Soda, and Borate Minerals	2,500
1475	Phosphate Rock	2,500
1476	Rock Salt	2,500
1477	Sulfur	1,000
1479	Chemical and Fertilizer Mineral Mining, Not Elsewhere Classified.	1,000
1481	Nonmetallic Minerals (Except Fuels) Services.	1,000
1492	Gypsum	1,000
1496	Talc, Soapstone, and Pyrophyllite	250
1499	Miscellaneous Nonmetallic Minerals, Not Elsewhere Classified.	250
Div. C	Construction	
	Major Group 15—Building Construction—General Contractors and Operative Builders	
1521	General Contractors—Single-Family Houses.	25
1522	General Contractors—Residential Buildings, Other Than Single-Family.	100
1531	Operative Builders	200
1541	General Contractors—Industrial Buildings and Warehouses.	500
1542	General Contractors—Nonresidential Buildings, Other Than Industrial Buildings, and Warehouses.	500
	Major Group 16—Construction Other Than Building Construction—General Contractors	
1611	Highway and Street Construction, Except Elevated Highways.	500
1622	Bridge, Tunnel, and Elevated Highway Construction.	500
1623	Water, Sewer, Pipe Line, Communication and Power Line Construction.	500
1629	Heavy Construction, Not Elsewhere Classified, Except Dredging[2].	500
1629	Dredging	1,000
	Major Group 17—Construction—Special Trade Contractors	
1711	Plumbing, Heating (Except Electric), and Air Conditioning.	80
1721	Painting, Paper Hanging, and Decorating.	50
1731	Electrical Work	50
1741	Masonry, Stone Setting, and Other Stonework.	50
1742	Plastering, Drywall, Acoustical and Insulation Work.	50
1743	Terrazzo, Tile, Marble and Mosaic Work.	25
1751	Carpentering	50
1752	Floor Laying and Other Floorwork, Not Elsewhere Classified.	80
1761	Roofing and Sheet Metal Work	60
1771	Concrete Work	50
1781	Water Well Drilling	50
1791	Structural Steel Erection	80
1793	Glass and Glazing Work	50
1794	Excavating and Foundation Work	50
1795	Wrecking and Demolition Work	50
1796	Installation or Erection of Building Equipment, Not Elsewhere Classified.	200
1799	Special Trade Contractors, Not Elsewhere Classified.	50
Div. D	Manufacturing[3]	
	Major Group 20—Food and Kindred Products	
2011	Meat Packing Plants	1,500
2013	Sausages and Other Prepared Meat Products.	200
2016	Poultry Dressing Plants	250
2017	Poultry and Egg Processing	500

Senator HAYAKAWA. One final question of Mr. Hahn. The evaluation of the adequacy of a small business to handle certain contracts, that is, whether it is capable of doing the work, this evaluation, I understand you to say, is repeated unnecessarily. After it has been done by one agency, let's say the Air Force or Navy does it all over again. Is that correct?

Mr. HAHN. That is correct, yes. The SBA has statutory authority to determine——

Senator HAYAKAWA. So the second evaluation is possibly illegal?

Mr. HAHN. There are people who believe it is. There is no statutory authority.

Senator HAYAKAWA. That is what you suggested.

Are you aware that the SBA recently proposed a policy that would virtually abolish certificates of competency if used for contracts under $10,000.

Mr. SEIDMAN. Yes. We feel that is a surprising move by the supposed protector of small business.

As you know, Public Law 95-507 reserves these contracts for small business concerns, under $10,000 contracts, if there are two or more responsible small business bidders. What this will do is lead to repeated findings that there are not two or more responsible small business bidders, and these contracts will end up going to the big boys instead of the small contractors for whom they have been reserved.

Senator HAYAKAWA. If there are any remaining questions, we will submit them to you in writing.

Thank you, gentlemen.

Our next witness will be the Hon. Donald E. Sowle, Administrator, Office of Federal Procurement Policy, Office of Management and Budget.

Will you please summarize your testimony? We will put the full testimony into the record immediately following your oral presentation.

STATEMENT OF HON. DONALD E. SOWLE, ADMINISTRATOR, OFFICE OF FEDERAL PROCUREMENT POLICY, OFFICE OF MANAGEMENT AND BUDGET

Mr. SOWLE. I would be very pleased to do that.

Senator HAYAKAWA. Thank you.

Mr. SOWLE. I am very thankful that you have invited me here today to testify on S. 2446. This administration, as stated by the President in his March 1982 report to the Congress on the State of Small Business, is "committed to assuring unrestricted access for small business to all segments of our economy."

In that same report, the President also noted that "contributions of small business to innovation and employment have been particularly noteworthy." Recently, the President signed Public Law 97-219, the Small Business Innovation Development Act of 1982, which provides for greater participation by small business in Government procurement of research and development. Implementation of the law is now in progress. We do not believe that enactment of S. 2446 would significantly enhance ongoing small business programs.

Section 5 of S. 2446 provides that each Federal agency shall review its procedure for awarding contracts for large systems and take all practicable steps to "subdivide the procurement contracts into smaller components on which small business concerns can compete."

The thrust of section 5 is already an integral part of procurement policy, and its enactment into law would not significantly, in our view, enhance the breakout program.

Section 6 of the bill would establish Government procurement contract arbitration panels. That was just discussed with the prior witnesses. We are not in favor of this section, either.

The purpose, of course, is to provide an opportunity for resolving disputes between any small business concern and any Federal agency. However, small businesses may already discuss disputed matters with contracting officials and other officials within the Federal Government.

Further, the Contract Disputes Act of 1978 sets forth small claims procedures as described earlier. Small companies are beneficiaries, if not the principal beneficiaries, of these expedited disputes procedures. We see no benefit in placing an additional disputes forum in the Small Business Administration. Such panels would add to the complexity of Federal procurement at a time when the administration is committed to simplifying the processes of Government.

The Small Business Procurement Advisory Committee that would be established by section 7 is an unneeded group that would at best duplicate the work of the regular SBA staff. If such a group is needed, SBA could establish one under present authority.

You invited me to present additional views beyond the scope of S. 2446. In this regard, Mr. Chairman, on a more positive note, I would like to direct your attention to our recently submitted Uniform Federal Procurement System proposal. This was required by Public Law 96-83. It is a comprehensive blueprint, and I would like to emphasize the word "blueprint," for procurement reform, both legislative and administrative, for the foreseeable future.

It would put procurement on a more organized, systematic basis than it has been up until now and provide the framework for numerous improvements in the process and for future changes in this dynamic field.

It should be of particular interest to this committee that Public Law 96-83 required OFPP to coordinate with the Small Business Administration in developing the procurement system proposal to insure that the needs of small businesses are fully considered and accommodated where possible.

Numerous features of the proposed system will particularly benefit small firms which now find it discouraging at best to cope with the voluminous, complicated regulations, solicitations, procedures, and contracts.

The proposal is based on four fundamental themes. I would just like to state those themes.

The first major theme is simplification of the procurement process. The second major theme of the proposal is enhanced and more effective competition. The third theme is increased professionalism in the procurement workforce. The final theme of the proposal is a management system which ties all of the above features into an integrated structure.

The management system includes an updated statutory base which outlines specific roles for OFPP and the agencies. The statutes also serve as a basis for single, Government-wide regulations.

Specific legislative proposals which incorporate the substance of the statutory reforms in the proposals were submitted to the Congress on the 30th of April of this year.

Many of the improvements contained in the administration's procurement system proposal can be accomplished, at least in part, without waiting for legislative changes. To initiate administrative actions, President Reagan issued Executive order 12352 on Federal Procurement Reforms on March 17, 1982. This Executive order requires each agency head to appoint a procurement executive who would have overall management responsibility for the procurement function in the agency.

One of our first actions under the order was to establish an executive committee for Federal procurement reforms. This committee is composed of the procurement executives from the eight largest procurement agencies, which covers about 96 percent of the dollars, plus representation from the Office of Personnel Management and from the Small Business Administration.

The executive committee, in turn, chartered several interagency task groups to develop guidance and recommendations to the agency heads in implementing the Executive order. The committee meets monthly to review the progress of the task groups, to provide counsel, and will continue for the foreseeable future to be a forum for discussion of procurement policy issues generally and procurement reform in particular.

Mr. Chairman, I appreciate the opportunity to testify here before you this morning. This concludes a summary of my statement.

Senator HAYAKAWA. Thank you, Mr. Sowle. I am very grateful to you for your testimony.

If I understand what you are saying, the Federal procurement system, the proposal for a Federal procurement system, will benefit small business probably more than S. 2446.

Mr. SOWLE. I think that is true, Mr. Chairman.

Senator HAYAKAWA. Would you outline very briefly why you think that is true?

Mr. SOWLE. Yes, sir. I think it is true for some probably 14 or 15 reasons. One of the very first ones was discussed here earlier this morning.

Senator HAYAKAWA. I realize S. 2446 still needs a lot of work.

Mr. SOWLE. Pardon?

Senator HAYAKAWA. I realize S. 2446 still needs a lot of work, but perhaps you think it ought to be abandoned altogether.

Mr. SOWLE. I think that is probably true. I think my full statement develops the reasons why we think it should be abandoned.

Senator HAYAKAWA. The central reason, if you could pick one, would be?

Mr. SOWLE. The central reason is that it does not really do anything for small business which is not already taken care of, either through the regulations or through current statutes.

Senator HAYAKAWA. What does the Federal procurement system do which the other legislation does not do?

Mr. SOWLE. That S. 2446 does not do?

Senator HAYAKAWA. Yes.

Mr. SOWLE. I am sorry, sir, but I do not understand your question.

Senator HAYAKAWA. What sections of FPS will specifically benefit small business?

Mr. SOWLE. The Federal procurement system, I cannot name off the sections to you, but there are parts of it which deal with many different things. As I mentioned, there are probably 14 or 15 different areas. I would like to discuss some of those for you very briefly.

First of all, we have a great effort underway which is covered in the proposal, in this blueprint, to simplify the whole procurement process. It would get rid of a lot of the paperwork, simplify solicitations, simplify contracts, raise the small purchase limitation so you can use the expedited procedures, and so forth.

Senator HAYAKAWA. Yes.

Mr. SOWLE. We have another whole area dealing with competition. Again, that was discussed by some of our predecessors here this morning.

The matter of sole source is really not covered by statute today. We feel that by changing the whole competitive structure to fit more what happens today and then put restrictions on sole source, small business will have a much better opportunity to participate in the Government's procurement programs.

We feel, also, that the appointment of contracting or procurement executives for each agency, and there can be as many procurement executives as the agency feels is necessary, is important. For example, the Department of Defense may feel that they must have several procurement executives at various levels, and an organization like the Department of Agriculture may not. The procurement executive really becomes a focal point for management of the entire system within a given agency. He would have responsibility for setting standards, procurement systems standards, for policies unique to the agency and regulations unique to the agency, for improvement of the work force, for seeing that solesource procurements are fully justified and follow the guidelines that will be set forth, and a whole series of management-type things that are not done today.

Even in the Defense Department, where they do have the acquisition executive, his focus is primarily on major systems. The procurement executive has much more responsibility and authority and accountability, which I think is something which has been missing in the past. Accountability for the actions of the procurement organization within any given agency is important.

Senator HAYAKAWA. You have said enough to indicate the direction in which you are looking. I will have to study your testimony more carefully and study S. 2446 again more carefully. If there are further questions to be asked of you, I shall submit them to you in writing.

Mr. SOWLE. All right, sir.

I would like to point out we do have lots of copies now of the so-called bluebook which is our proposal. If you have staff members interested in having more copies of that, we would be pleased to furnish it.

Senator **Hayakawa**. Thank you very much, Mr. Sowle. I am grateful to you for your testimony.

[The prepared statement of Mr. Sowle follows:]

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

OFFICE OF FEDERAL
PROCUREMENT POLICY

HOLD FOR RELEASE UNTIL DELIVERY
Expected at 10:00 a.m.
Thursday, September 16, 1982

STATEMENT BY THE
HONORABLE DONALD E. SOWLE
ADMINISTRATOR FOR FEDERAL PROCUREMENT POLICY
OFFICE OF MANAGEMENT AND BUDGET
BEFORE THE COMMITTEE ON SMALL BUSINESS
UNITED STATES SENATE
SEPTEMBER 16, 1982

Mr. Chairman and Members of the Committee:

Thank you for inviting me to testify this morning on S. 2446. This Administration, as stated by the President in his March 1982 Report to the Congress on the State of Small Business, is "committed to assuring unrestricted access for small business to all segments of our economy." In that same Report, the President also noted that "contributions of small business to innovation and employment have been particularly noteworthy". Recently, the President signed Public Law 97-219, the Small Business Innovation Development Act of 1982, which provides for greater participation by small business in Government procurement of research and development. Implementation of the law is in progress. We do not believe that enactment of S. 2446 would significantly enhance ongoing small business programs.

Section 5 of S. 2446 provides that each Federal agency shall review its procedure for awarding contracts for large systems and take all practicable steps to "subdivide the procurement contracts into smaller components on which small business concerns can compete". The general subject of breakouts covers two separate but related areas: (a) component breakout and (b) DOD High Dollar Spare Parts Breakout Program, both of which are discussed in the Defense Acquisition Regulation (DAR). Most of the opportunity for breakout occurs in the Department of Defense, so I will discuss breakout in the context of DOD procurement. Component breakout involves, in the language of the DAR, the general area of "decisions on whether or not components should be purchased by the Government directly and furnished to an end item contractor as Government-furnished material, for incorporation in the end item." Defense Acquisition Regulations state that it is DOD policy to break out a component, if certain conditions involving the lack of competition are present. Therefore, the thrust of section 5 of S. 2446 is already an integral part of procurement policy, and its enactment into law would not significantly enhance the breakout program.

The "DOD High Dollar Spare Parts Breakout Program" was, as you probably know, the subject of a recent GAO report (B-207831, August 2, 1982). In that report the GAO concluded that the "SBA breakout efforts contributed significantly toward improving the Air Force's breakout program" and that "opportunities exist to improve the effectiveness of the spare parts breakout program and to realize even greater breakout accomplishments." Finally the GAO concluded, with respect to the four Air Logistics Centers surveyed, that "In spite of difficulties posed by the lack of technical data, SBA's breakout efforts have resulted in large dollar savings in relation to the program's costs. Although the breakout specialists used some questionable methods to compute their savings, we believe they contributed to most of the breakouts reviewed. We also believe that SBA may actually be saving the Government more money than its reports indicate."

We believe that even further improvement could be achieved through the assignment of additional technical personnel to the breakout program. The DAR provides that the project or program manager, supported by a team of Government specialists including the Small Business Specialist, will be responsible for "Component Breakout Selection, Review and Decisions." The Small Business Specialist serves as the principal advocate for small business. The Small Business Specialist, however, is rarely technically qualified or trained to discuss technical and program breakout matters with the program manager or "cognizant engineering personnel.' In our opinion, the component breakout program would be of more assistance to small business if a qualified engineer or technical person, from among existing resources, were assigned to serve on the breakout team as an advocate for small business.

We do not favor the establishment in the Small Business Administration of "Government procurement contract arbitration panels" as detailed in section 6. These panels would "provide an opportunity for resolving disputes between any small business concern and any Federal agency having procurement authority concerning any Government procurement contract which is let to such concern or which may be let to such concern." Small businesses (and all other businesses) may now discuss disputed matters with the contracting offices or other officials. It is only after failure to resolve a dispute that the matter is appealable to an agency board of contract appeals. Further, the Contract Disputes Act of 1978 sets forth small claims procedures (a "summary" procedure for claims under $10,000 and an "accelerated" procedure for claims under $50,000) under which disputes are resolved in four months (summary procedure) or six months (accelerated procedure). While we recognize that not all claims and disputes of small companies are under $50,000, many of them are. Thus, small companies are beneficiaries - if not the principal beneficiaries - of these expedited disputes procedures. The arbitration panels would also be authorized to hear disputes about contracts "which may be let." As to this type of dispute, the General Accounting Office has traditionally been available to small companies which believe they have been treated unfairly in the bidding and award process by a procuring agency. In sum, we see no benefit in placing an additional disputes forum in the Small Business Administration, as proposed by this bill. Such panels would add to the complexity of Federal procurement at a time when the Administration is committed to simplifying the processes of Government.

Further, we believe that the Small Business Procurement Advisory Committee that would be established by section 7 is an unneeded group that would, at best, duplicate the work of the regular SBA staff. If such a group is needed, SBA could establish one under present authority. Accordingly, additional legislation is not needed.

One other area I want to discuss is small business set-asides under section 15 of the Small Business Act. The section 15 set-aside program, in effect since the late 1950's, is a mainstay of the Government's efforts to assist small business in obtaining a larger share of Federal procurement dollars. In FY '81, for example, the awards to small business under the set-aside program totalled approximately 10.6 billion. Section 15 provides an appeal mechanism to resolve differences between agency procurement and SBA personnel. Progress indicates that the present system is effective and maintains the proper balance between the agency's mission and small business considerations. The making of set-asides is extremely important to increasing the small business share of Federal procurement, and we believe it is working reasonably well.

You invited me to present additional views beyond the scope of S. 2446. In this regard, I would like to direct your attention to our recently submitted Uniform Federal Procurement System (UFPS) proposal, which was required under section 6 of P.L. 96-83. This proposal, which was presented to the Congress on February 26, 1982, is the culmination of more than a dozen years of exhaustive study of the procurement process. It is a comprehensive blueprint for procurement reform, both legislative and administrative, for the foreseeable future. It would put procurement on a more organized, systematic basis than it has been up to now, and provide the framework for numerous improvements in the process, and for future changes in this dynamic field.

The proposal was based on four fundamental themes. I would like to touch on each of these briefly. The first major theme is simplification of the procurement process. This will make it easier for those who contract for the government as well as for those who do business with the government, encourage more firms to seek government business, and make procurement more responsive in filling the needs of the user. A variety of measures will contribute to simplification.

One of these is more timely availability of funds and greater flexibility in the use of funds, particularly in funding continuing requirements that cross over fiscal years. Some others are: expressing needs in terms of function or desired performance rather than predetermined solutions; a single government-wide regulation; eliminating unnecessary contract provisions; raising the small purchase ceiling; and greater use of imprest funds.

A second major theme of the proposal is enhanced and more effective competition.

Formal advertising, by law, is the preferred method of procurement, but it is used today for less than 10 percent of the dollars involved in federal procurement. The rigid requirements of formal advertising tend to inhibit the government from taking advantage of the competitive marketplace. It requires detailed specifications and terms and conditions which permit awards solely on the basis of price.

Most government requirements cannot be described using this method since detailed specifications do not generally exist and it would be too costly to develop and maintain them. As a result, the number of suppliers tends to shrink, in those instances where detailed specifications are available, to those few -- or in some cases only one -- who perform to unique government specifications. The government often becomes the sole or major customer of these contractors.

Negotiation, under one of the 17 exceptions in the Armed Services Procurement Act or one of 15 in the Federal Property Act, has become the rule in government procurement. We discussed in our February proposal some fundamental changes in the approach to competition. Basically, we propose eliminating the current requirements either to use formal advertising or justify negotiation, and to make procurement either competitive or noncompetitive. There would be an absolute preference for competition and two equally valid methods of competitive procurement -- bidding with discussion and bidding without discussion. Award could be made on the basis of price, the lowest total cost to the government or multiple factors such as technical excellence, small business and labor surplus considerations, etc.

Noncompetitive procurement would still have to be justified and would be subject to stricter controls than exist today. However, the negotiation exceptions and the onerous requirement for determinations and findings would be eliminated. Contracting officers would have more flexiblity in choosing the type of competition and method of bidding, but they would also be accountable for the results.

A third theme of the proposal is increased professionalism of the procurement work force. The proposed system envisions a more responsible role for procurement personnel than they have generally had in the past. This will be particularly important in connection with the new concepts of competition which will require greater initiative and judgment by contracting officers. Furthermore, the wider use of functional and performance type specifications will require a greater knowledge of the marketplace and closer involvement in developing procurement strategies through better procurement planning.

Ensuring an adequate professional work force to meet those responsibilities will require attention to all phases of career management, such as establishing qualifications and classification standards, recruitment, training, education and experience. It will also require an acceptance by other disciplines which play a role in the procurement process as contracting officers and personnel assume a more responsible role.

The final theme of the proposal is the management system which ties all of the above features into an integrated structure. The management system includes an updated statutory base which outlines specific roles for OFPP and the agencies. The statutes also serve as a basis for a single, government-wide regulation. The key individual in the procurement management structure is a procurement executive, the focal point in each agency for the flow of authority, responsibility and accountability in the management of procurement.

The procurement executive will also be the focal point for coordination with OFPP in developing government-wide standards for the procurement system, and in developing government-wide procurement policies.

Specific legislative proposals, which incorporate the substantive statutory reforms contained in the proposals, were submitted to the Congress on April 30, 1982.

It should be of particular interest to this Committee that Public Law 96-83 required OFPP to coordinate with the Small Business Administration in developing the procurement system proposal, to ensure that the needs of small businesses were fully considered and accommodated. Numerous features of the proposed system will particularly benefit small firms which now find it discouraging at best to cope with voluminous and complicated regulations, solicitations and contracts.

The requirements for advance planning, market research, greater use of functional specifications and more widespread purchase of commercial off-the-shelf products, will enhance the opportunity for small firms to participate in the government market.

Simplified solicitations and uniform Government-wide formats for solicitation and contract documents will enable contracting officers, contractors, and prospective contractors alike to look in the same section of every solicitation or contract to find the statement of work, applicable clauses, the delivery and payment schedule and other information. Special simplified formats will be tailored for such areas as small purchases and commercial products or services. Small purchases by the Government are very important to small businesses. The UFPS would greatly simplify such purchases which, in Fiscal Year 1981, totalled 17.6 million transactions below $10,000. The proposed system would remove from the small purchase procedure many of the same legislative and regulatory requirements that complicate the procurement process in general. A single, simplified Government-wide regulation will make it easier for business firms to cope with the procurement process. More timely payments and greater use of imprest funds should ease the cash flow burdens of small firms.

We also believe that specific consideration should be given to a procedure suggested to us by a small business concern whereby all certifications, representations, agreements to procedures, etc. could be given by a small business annually to one control point in the Federal Government. In turn, this control office might issue to the small businesses a certification or evidence that the required representations, terms and conditions had been complied with. This could represent a significant savings in time and effort for both the small business and the Federal Government.

Many of the improvements contained in the Administration's procurement system proposal can be accomplished, at least in part, without waiting for legislative changes. To initiate administrative actions, President Reagan issued Executive Order 12352 on federal procurement reforms on March 17, 1982.

This Executive Order required each agency head to appoint a Procurement Executive and sets forth the principal administrative reforms called for by the proposal. The Procurement Executive would have overall management responsibility for the procurement function in the agency. The qualifications and authority of the Procurement Executive are a key element in the success of our procurement reform efforts.

One of our first actions under the order was to establish an Executive Committee on Federal Procurement Reforms, composed of the Procurement Executives from the eight largest procuring agencies, plus representation from the Office of Personnel Management and from the Small Business Administration. The Executive Committee in turn chartered several interagency task groups to develop guidance and recommendations to the agency heads in implementing the Executive order. The Committee meets monthly to review the progress of the task groups, and will continue for the foreseeable future to be a forum for discussion of procurement policy issues generally.

Thank you for the opportunity to testify. This concludes my prepared statement. I will be pleased to respond to any questions you may have.

Senator HAYAKAWA. Our next witness is Mr. Robert McDermott, Associate Administrator for Procurement and Technical Assistance, Small Business Administration.

STATEMENT OF ROBERT F. McDERMOTT, ASSOCIATE ADMINISTRATOR FOR PROCUREMENT & TECHNICAL ASSISTANCE, SMALL BUSINESS ADMINISTRATION

Mr. McDERMOTT. In keeping with your request, Mr. Chairman, I will summarize what is already a rather short statement and request that my complete statement appear in the record.

Senator HAYAKAWA. Thank you.

Mr. McDERMOTT. I am pleased to appear before your committee this morning, Mr. Chairman, to provide you with the views of the Small Business Administration on S. 2446, the Small Business Procurement Reform Act of 1982.

I wish to commend Senator Specter and the cosponsors of this bill for bringing several important small business procurement issues to the attention of the Congress. Although SBA disagrees with some of the particular remedies proposed in the legislation, we feel that the bill is an important step in proposing solutions that deal with important and difficult problems.

The bill will make several changes in the Small Business Act. It will require SBA's Administrator to take several steps.

At the committee's request, I shall not address section 4 in my testimony. The committee has already acted upon that section.

The bill would require heads of procuring agencies to review their procedures for awarding contracts for large procurements on which small businesses cannot compete, and take all practicable steps to subdivide them into smaller components on which small businesses can compete. The issue of subdivision of contracts is one on which SBA has favorably testified and one which SBA continues to advocate. We welcome this attempt to statutorily encourage subdivision.

The bill would also allow SBA's Administrator to establish panels to arbitrate disputes between a small contractor and a procuring agency on contracts let or to be let to the contractor. A decision by such a panel would be binding only to the extent that the parties agreed it would be. In our opinion this virtually assures that any such SBA arbitration panels would rarely, if ever, be convened.

Additionally, the provisions of this subsection would necessitate amendments to other statutes and all Federal agency acquisition regulations dealing with resolution of disputes between Government contracting officials and contractors. You already heard about that earlier this morning.

Finally, the bill would establish a Small Business Procurement Advisory Committee to advise Congress and SBA's Administrator on matters relating to Government procurement contracts awarded to, or set aside for, small business concerns. At the close of each calendar year, the committee would report to the Administrator and the Congress on means of increasing Government contracts awarded to small business.

We recommend that the activities of any such committee be directed at the latter purpose solely. SBA's concerns and energies, in fact, should be and are devoted almost totally to those procurement requirements which Federal agencies do not provide the small business sector equitable opportunity to compete for and supply, rather than to those which are awarded or are about to be awarded to small concerns.

Alternatively, to avoid the creation of yet another statutorily mandated advisory committee, we would be willing to give this responsibility to the existing subcommittee on procurement assistance of SBA's National Advisory Council.

Overall, we at SBA endorse the intent of S. 2446, and again wish to commend its sponsors for bringing these issues to the attention of the Congress.

Mr. Chairman, this concludes my summary of the prepared statement. I will be pleased to attempt to answer any questions you may have.

Senator HAYAKAWA. Thank you very much, Mr. McDermott.

[The prepared statement of Mr. McDermott follows:]

SBA U.S. Small Business Administration Washington, DC 20416

STATEMENT OF
ROBERT F. McDERMOTT, ASSOCIATE ADMINISTRATOR FOR
PROCUREMENT & TECHNICAL ASSISTANCE
SMALL BUSINESS ADMINISTRATION
BEFORE THE
COMMITTEE ON SMALL BUSINESS
UNITED STATES SENATE

SEPTEMBER 16, 1982

MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE:

I am pleased to appear before your Committee, Mr. Chairman, to provide you with the views of the Small Business Administration on S. 2446, the Small Business Procurement Reform Act of 1982. This legislation was introduced by Senator Specter on April 28 with Senators Weicker, Nunn, Baucus, Dixon, Glenn, Hayakawa, Packwood, and Riegle as cosponsors.

I wish to commend Senator Spector and the cosponsors of this bill for bringing several important small business procurement issues to the attention of the Congress. Although SBA disagrees with some of the particular remedies proposed in the legislation, we feel that the bill is an important step in proposing solutions that deal with important and difficult problems.

The purposes of the bill are:

1) to assure further that a fair proportion of government procurement contracts are awarded to small business concerns and to increase small business participation in procurement where possible;

2) to simplify the contracting procedures of the United States which relate to small business;

3) to establish arbitration panels to resolve disputes which arise between small business concerns and Federal agencies concerning government procurement contracts; and

4) to establish a Small Business Procurement Advisory Committee to make legislative and administrative recommendations concerning government procurement contracts for small business concerns and to provide better representation of small business concerns before the Congress and SBA.

To accomplish these purposes, the bill would make several changes in the Small Business Act, and it would require SBA's Administrator to take several steps. At the Committee's request, I shall not address Section 4 in my testimony, since the Committee has already acted upon that section.

The bill would require heads of procuring agencies to review their procedures for awarding procurement contracts for large procurements on which small businesses cannot compete, and take all practicable steps to subdivide them into smaller components on which small businesses can compete. The issue of subdivision of contracts is one on which SBA has favorably testified and one which SBA continues to advocate. We welcome this attempt to statutorily encourage subdivision.

The bill would also allow SBA's Administrator to establish panels to arbitrate disputes between a small contractor and a procuring agency on contracts let or to be let to the contractor. A decision by such a panel would be binding only to the extent that the parties agreed it would be. In our opinion this virtually assures that any such SBA arbitration panels would rarely, if ever, be convened. Additionally, the provisions of this subsection would necessitate amendments to other statutes and all federal agency acquisition regulations dealing with resolution of disputes between government contracting officials and contractors. Examples include: the Contract Disputes Act of 1978; existing federal agency boards of contract appeals procedures; and the statutory rights of government contractors and prospective government contractors to seek relief on federal procurement matters through the U.S. Comptroller General and Court of Claims, etc.

Finally, the bill would establish a Small Business Procurement Advisory Committee to advise Congress and SBA's Administrator on matters relating to government procurement contracts awarded to, or set aside for, small businesses concerns. At the close of each calendar year, the Committee would report to the Administrator and Congress on means of increasing government procurement contracts awarded to small businesses. We recommend that the activities of any such Committee be directed at the latter purpose. SBA's concerns and energies, in fact, should be and are devoted almost totally to those procurement requirements which federal agencies do not provide the small business sector equitable opportunity to compete for and supply, rather than to those which are awarded to small concerns. Alternatively, to avoid the creation of yet another statutorily-mandated advisory committee, we would be willing to give this responsibility to the existing subcommittee on procurement assistance of SBA's National Advisory Council.

Overall we endorse the intent of S. 2446, and wish to commend its sponsors for bringing these issues to the attention of the Congress.

Mr. Chairman, this concludes my prepared statement. I will be pleased to answer any questions.

Senator HAYAKAWA. I am fascinated with your idea, as you state on page 3 of your testimony, of taking all practicable steps to subdivide large procurements into smaller components on which small businesses can compete. Is this practical?

Mr. McDERMOTT. Yes, it is, sir.

Senator HAYAKAWA. It can be done efficiently? After all, the large businesses to which it could otherwise be sent would have to subdivide it themselves in order to take care of the order, would they not?

Mr. McDERMOTT. That is true. However, what the large business would do would be to decide what it in fact was going to make as opposed to what it was going to buy.

Senator HAYAKAWA. Yes.

Mr. McDERMOTT. Then what it could not make or, for one reason or another, at the moment did not wish to make, it could subcontract to other business, both large and small, as it wished.

Our direction in this area in the past has been to attempt to take some of these major procurements and take components of those out of the total buy, and be able to reserve that buy for small business if possible, or, if not that way, at least open it to competition, and therefore probably reduce price and increase competition.

Senator HAYAKAWA. Thank you. That is a fascinating idea.

I am distressed to learn that small business participation on Federal contracts is way down this year. To what do you attribute this decline? What can be done during the remainder of the year and the coming years to bring small business participation up to an acceptable level?

Mr. McDermott. I am not aware, Senator, that it is way down this year. The last statistics I saw were half-year statistics. I believe at that time there was a slight increase over the same period last year.

Senator Hayakawa. You are not aware that it is down this year?

Mr. McDermott. I say the last statistics I saw were for the end of the half-year. It was up for over a similar period of last year.

There has been a decline in the past 2 fiscal years, that is true. We attribute that to a number of things. It has been proven over the years that when the SBA representatives, Procurement Center Representatives, are not in fact engaged in the review of upcoming requirements of procuring agencies that the percentage of awards to small business has declined.

As a result of the enactment of Public Law 95-507 and its subcontracting requirements, we have for the last 2 years had our Procurement Center Representatives reviewing proposed subcontracting plans in addition to their normal function of making small business setasides, attempting to split up large buys, and so on.

Unfortunately, in some instances, these individuals are spending as much as 80 percent of their time reviewing proposed subcontracting plans. It is our opinion that this is one reason, perhaps a major reason, that there has been a decline in small business percentages.

We are looking at that to determine what we can do to overcome that situation. We have to make a change there somewhere.

Of course, the other thing that has to be considered is what it is that the Government is buying. There has been an increase in some of those types of things where small business overall cannot manufacture them.

Senator Hayakawa. Thank you. This is something I have to clear up in my own mind. What is the difference between components breakout and spare parts breakout?

Mr. McDermott. A very significant difference, sir. When we talk of component breakout——

Senator Hayakawa. There are many things a Ph. D. in English cannot understand. This is one of them. [Laughter.]

Mr. McDermott. There are all sorts of things I don't understand, either, sir, but I think I understand the difference between component and spare parts breakout.

Component breakout, that is what S. 2446 addresses. It is where you have a major system. Take, for example, the B-1 bomber. There is no small business that can manufacture the B-1 bomber.

Senator Hayakawa. That is right.

Mr. McDermott. However, there are many small businesses that can manufacture components of that B-1 bomber.

Component breakout to us means taking various segments of that B-1 bomber prior to its coming into the procurement phase, breaking those out of the system, breaking those away from the B-1 bomber procurement, and hopefully being able to reserve or set-aside procurements for those components for small business. If not that, at least being able to open procurements of those components up for competition would be our hope.

Spare parts breakout is different in that we are looking at something much further down the road where, in fact, the Government is buying the spare or replenishment parts to continue to maintain those items which are already in the inventory. If we had bought a B-1 bomber and it were flying, we would have to buy spare parts and maintenance parts to maintain that aircraft. Those are the two basic differences.

What you heard earlier this morning from some of our previous witnesses had to do with the spare parts breakout program. That is where we have been moving and we hope to continue to move and make inroads.

Senator HAYAKAWA. They were not really talking about components.

Mr. McDERMOTT. The bill talks about component breakout. The report from the General Accounting Office, and what the gentlemen this morning talked about, was about spare parts breakout.

Senator HAYAKAWA. I see.

Is it your recommendations we move more energetically in both directions?

Mr. McDERMOTT. We are very happy to see that the proposed legislation would, in fact, give a statutory base to the component breakout. We would like also to see the spare parts breakout included in that statutory base.

However, apart from that, we are working diligently in an attempt to get into that process and to continue our entrance into that process. Statutorily it would help.

Senator HAYAKAWA. It would be desirable, then, to bring the whole spare parts matter into the Specter bill?

Mr. McDERMOTT. I would say so. It is at present covered by a regulation within the Department of Defense. However, there is no statutory base that I know of.

Senator HAYAKAWA. I will study your testimony further. I want to thank you for being with us this morning.

If there are further questions, I shall submit them to you in writing. We shall have some questions for you in writing.

Mr. McDERMOTT. Thank you, Mr. Chairman.[1]

Senator HAYAKAWA. Next is Mr. Robert M. Gilroy, Senior Associate Director of Procurement, Logistics and Readiness Division, U.S. General Accounting Office.

Welcome, Mr. Gilroy.

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[1] Information not available at time of going to press.

STATEMENT OF ROBERT M. GILROY, SENIOR ASSOCIATE DIRECTOR OF PROCUREMENT, LOGISTICS AND READINESS DIVISION, U.S. GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY SIDNEY WOLIN, GROUP DIRECTOR, GENERAL PROCUREMENT GROUP; GWENDOLYN R. JAFFE, SUPERVISORY AUDITOR, GENERAL PROCUREMENT GROUP; AND JERRY REEDER, SUPERVISORY AUDITOR FOR KANSAS CITY OFFICE

Mr. GILROY. Thank you, Mr. Chairman.

Senator HAYAKAWA. I see you brought an adequate bodyguard.

Mr. GILROY. General support staff, sir.

Senator HAYAKAWA. You cannot be too careful nowadays. [Laughter.]

It will be a pleasure to hear from you, Mr. Gilroy. I would be grateful if you would try to summarize your statement if it is long. In any case, the full statement will be put into the record.

Mr. GILROY. All right, sir. I would like first to introduce my associates. On my immediate right is Sid Wolin, Group Director of Procurement, Logistics and Readiness Division. On my far left is Jerry Reeder from our Kansas City regional office, who has done work on breakout at Tinker Air Force Base at Oklahoma City Air Logistics Center. On my immediate left is Gwendolyn Jaffe, who has done a lot of our work in 8(a) programs, and small business procurement concerns. 157-61—A736A.018

Senator HAYAKAWA. Welcome to all three of you.

Mr. GILROY. I have an abbreviated statement that I would like to read at this time.

Senator HAYAKAWA. If you please.

Mr. GILROY. I have a more detailed statement which I shall submit for the record.

Senator HAYAKAWA. Proceed.

Mr. GILROY. I am pleased to appear here today to discuss our assessment of certain efforts by the Small Business Administration to identify new competitive contracting opportunities for procurement of aircraft spare parts by the Air Force. As you may know, we performed this work at the request of Congressman Joseph P. Addabbo, a member of the House Small Business Committee, and issued our report on August 2, 1982.

SBA has procurement center representatives at 52 Federal acquisition centers. Additionally, since late 1979, a SBA breakout PCR has been assigned to work at the Air Force Air Logistics Centers in San Antonio, Tex.; Oklahoma City, Okla.; and Warner Robins, Ga. Their primary mission has been to challenge spare parts procurements that the Air Force plans to make on a noncompetitive basis—primarily from large business prime contractors who supply the major end items—and to attempt to identify ways to purchase the parts on a competitive basis, or, at a minimum, directly from the part's actual manufacturer.

We looked at the activities and reported accomplishments of the breakout PCR's during fiscal years 1980 and 1981. Additionally, in our review, we examined the breakout efforts of the Odgen ALC's regular PCR for the same period because he was reporting substantial breakout accomplishments, even though breakout was not his primary function.

During this 1980 to 1981 period, SBA reported 294 breakout actions at the four ALC's and related savings of $7.3 million. We tested 71 of the largest reported savings totaling $3.5 million. Although we found some problems with the methodology and rationale for estimating some of the savings, we concluded that SBA could reasonably claim credit for successfully breaking out 50 of the parts, involving reported savings of about $2.4 million; 42 of the 50 breakouts, totaling over $1.5 million, were awarded to small businesses, while 8 breakouts, totaling nearly $900,000, were awarded to large businesses. Specific details for each ALC are included in the attachments. Competition—two or more offerors—was introduced in 41 of these 50 procurements.

We did not agree with SBA's claimed savings on 21 of the cases. In most of these cases the Air Logistics Center had either previously procured the part from the source identified by SBA or had already broken the part out for competition, but had failed to update its records.

SBA's reported savings, however, could very well understate actual breakout accomplishments. SBA officials have reported they are sometimes unable to calculate savings on subsequent purchases of items already broken out because of limited time and staff.

An example of how the participation of an SBA breakout PCR can result in a successful breakout follows:

The San Antonio ALC had been buying tube assemblies directly from the prime contractor since 1978. In August 1980, the Air Force issued a purchase request coded 3L, low dollar procurement noncompetitive, and solicited a bid only from the prime contractor. The SBA breakout PCR challenged the procurement method code. In response to this challenge, procurement officials at the San Antonio ALC recoded the procurement 3H, incomplete data package. The breakout PCR again challenged the code. Procurement officials at the ALC then found the drawing in question, recoded the procurement for open competition, and issued a new purchase request. The subsequent purchase of 661 units was competitively awarded to a small business at a price which was about $181 per unit lower than the price bid by the prime contractor and about $321 per unit less than the prime contractor's original sole-source bid in August 1980. The Air Force thus paid $212,498 less to buy the tube assemblies competitively than if the prime contractor's original sole-source bid had been accepted.

Unfortunately, breakout progress has been, and will continue to be, slow unless the Air Force finds ways to effectively deal with a number of constraints which have hampered breakout efforts. These include:

Incomplete information on who actually manufactures the parts for the prime contractor.

Missing technical data with uncertainties as to whether data may be available elsewhere.

Questions of whether the data is proprietary, and therefore legally unavailable to other suppliers.

Reluctance on the part of ALC material management officials to accept the additional risk and inconvenience in procuring from a new source.

In spite of difficulties posed by these constraints, SBA's breakout efforts have resulted in large dollar savings relative to the program's costs. SBA's breakout efforts have also increased DOD's awareness of potential savings through breakout and have helped the Air Force identify new opportunities to obtain competition.

Within the next year, SBA would like to expand the breakout program by assigning breakout PCR's to a number of additional installations. We strongly support this action since effective use of these additional breakout PCR's should result in even greater savings to the Government.

Mr. Chairman, this completes my prepared statement. We would be pleased to respond to any questions you or other members of the committee have at this time.

Senator HAYAKAWA. Thank you very much, Mr. Gilroy.

You say at the end that you would like to see this kind of program extended to a number of other additional installations.

Mr. GILROY. Yes, sir.

Senator HAYAKAWA. Where are the installations you have been talking about?

Mr. GILROY. SBA breakout specialists are currently operating at three Air Force air logistics centers. We are talking about expanding this program to other installations. They could be Army, Navy, or any large acquisition installation.

Senator HAYAKAWA. But the Air Force as a whole has to be taken care of by these three?

Mr. GILROY. Other air logistics centers. They have procurement center representatives, but this one is a specialist. This is a procurement center representative who is also a breakout specialist. We have them currently at Oklahoma City, San Antonio, and Warner Robins.

The procurement center representative at Ogden does the breakout but it is not his particular specialty. His efforts were included in our statistics because he was very successful in what he did.

An air logistics center is located at Sacramento, making a total of five air logistics centers. The Air Force is covered at four of the five logistics centers.

Senator HAYAKAWA. You are recommending that analogous offices should be set up for——

Mr. GILROY. Army, Navy.

Senator HAYAKAWA. And everybody else? All the Armed Forces?

Mr. GILROY. Yes.

Senator HAYAKAWA. They do not have them?

Mr. GILROY. There are 52 procurement center representatives at various buying areas. Only a small part of their function is breakout. We would like to see greater use of the breakout specialists, whose primary mission is breakout.

Senator HAYAKAWA. It does save money?

Mr. GILROY. From what we have seen, it definitely does.

Senator HAYAKAWA. Then they should be established for all the services as well as the Air Force. It would then amount to considerable savings to the taxpayer?

Mr. GILROY. Based on what we have seen in our limited sample, it would seem worth the effort to increase the number of breakout specialists.

Senator HAYAKAWA. And the amount of breakout being done now in the other services is done, incidentally, without a systematic bureaucracy which dedicates itself specifically to this purpose?

Mr. GILROY. I should add there are programs in existence. The Air Force is one we are familiar with. The Air Force has its own breakout program which is in addition to the small business program. We believe at times they work well, hand-in-hand.

The Air Force is trying to get their breakout specialists to increase competition. In this process small business benefits. Small business specialists will breakout items for small business and increase its competition, so they work hand-in-glove.

We would like to see a greater effort on the part of the Air Force and the other services in breaking out parts for competitive procurement, either going back to the actual manufacturer or going competitively, where other than the actual manufacturer could compete.

Senator HAYAKAWA. So, the ultimate aim of the efforts of all of you is more efficient use of the taxpayers' money.

Mr. GILROY. Exactly.

Senator HAYAKAWA. Fine.

In your opinion does spare parts breakout slow down the acquisition process?

Mr. GILROY. I might want to defer to Jerry Reeder, who can perhaps tell us better. A lot of it is how well the initial procurement is organized. A code is assigned to each procurement. This code is designed to show how the part can be bought.

During the procurement process, the breakout procurement center representative takes a look at this code to determine whether the part is unnecessarily restricted, meaning it may have to be bought sole source. The breakout PCR makes an effort to see whether the part can be competed for less or if the actual manufacturer can be identified.

That process takes time. I will defer to Mr. Reeder to tell us whether it significantly delays the process.

Senator HAYAKAWA. Mr. Reeder, I invite your comments. I also invite comments from the rest of the panel whenever they have something they want to get off their chests.

Mr. REEDER. Breaking out a part would not significantly delay the process. If the data were there and the engineering resources were there, and the cooperation that is needed was there, I do not feel the breakout program would significantly delay the procurement process.

Senator HAYAKAWA. You do not believe it will delay it?

Mr. REEDER. If it worked as it was setup to work. The problem is that so much of the time the information needed to breakout a part is not available.

Senator HAYAKAWA. Why is it not available?

Mr. REEDER. It was not obtained during the initial acquisition.

Senator HAYAKAWA. When you get a complex piece of machinery, such as an aircraft, does it not come with a parts manual as well as a huge book describing all its insides and what goes into it? Does that not contain information as to where these parts come from?

Mr. **Reeder**. That would be very desirable, yes. That is not the way it usually works.

Senator **Hayakawa**. You list several constraints on breakout efforts at Air Force installations. Do you have any suggestions for ways in which the SBA or the Air Force can alleviate these constraints? What are some of these constraints?

Mr. **Gilroy**. We intend, as we say in our report which we sent to Mr. Addabbo a couple months ago, to follow up to see what we can do about these constraints. The constraints are basically: (1) Incomplete information on who actually manufactured the parts for the prime contractor; (2) the missing technical data with uncertainties as to whether data may be available elsewhere; (3) questions as to whether data is proprietary and legally unavailable to other suppliers; and (4) reluctance on the part of the ALC material management officials to accept the additional risk and inconvenience of procuring from a new source.

On the last one, Mr. Reeder has recently informed me that the Air Force has taken a more aggressive approach, at least at Tinker Air Force Base, in trying to breakout parts, but we feel strongly that this needs much more attention from a lot higher authority than Tinker Air Force Base if we are to focus the attention needed.

We see an absence of perhaps upfront communication. The logistics people buying the spare parts should perhaps be in communication and coordination earlier with the acquisition people who are initially buying. I believe I heard Mr. McDermott on the reference to the B-1. This would be later supported by one of the air logistics centers.

If there were greater coordination up front with the acquisition people, perhaps you would have greater identification as to who actually manufactures some of the parts, which you will have to buy later at the logistics centers.

Senator **Hayakawa**. Again, I invite comments from any of you on this question. Do you have any thoughts on the component breakout provisions contained in S. 2446?

Mr. **Gilroy**. Again, up front we have not submitted S. 2446 to any kind of critical review. We have mainly addressed this report to Mr. Addabbo.

We have found the language in section 5 of S. 2446 quite similar to language which already exists and is planned for the new Federal acquisition regulation referred to as FAR.

We would encourage any kind of legislation which would help small business and increase competition because we believe this does result in a better price to the Government, so in that sense we would support S. 2446, with the reservation that section 5 seemed to us quite vague and seemed to us quite similar to language which already exists in the defense acquisition regulation and FAR.

Senator **Hayakawa**. Do any others have comments?

Mr. **Gilroy**. Apparently not.

Senator **Hayakawa**. We shall study your testimony. If there are further questions, we shall submit them to you in writing, Mr. Gilroy.

Mr. **Gilroy**. Yes, sir.

Senator **Hayakawa**. Meanwhile, thank you very much for being here and presenting your testimony and giving us the benefit of your experience.

Mr. **Gilroy**. We are happy to be here, sir.

[The prepared statement of Mr. Gilroy follows:]

STATEMENT OF

ROBERT M. GILROY, SENIOR ASSOCIATE DIRECTOR
PROCUREMENT, LOGISTICS, AND READINESS DIVISION

Mr. Chairman:

I am pleased to appear here today to discuss our assessment of certain efforts by the Small Business Administration (SBA) to identify new competitive contracting opportunities in the procurement of aircraft spare parts by the Air Force. As you may know, we performed this work at the request of Congressman Joseph P. Addabbo, a member of the House Small Business Committee, and issued our report on August 2, 1982.

SBA has Procurement Center Representatives (PCRs) at 52 Federal acquisition centers. Additionally, since late 1979, an SBA breakout PCR has been assigned to work at the Air Force Air Logistics Centers (ALCs) in San Antonio, Texas; Oklahoma City, Oklahoma; and Warner Robins, Georgia. Their primary mission has been to challenge spare parts procurements that the Air Force plans to make on a noncompetitive basis--primarily from large business prime contractors who supply the major end items--and to attempt to identify ways to purchase the parts on a competitive basis, or, at a minimum, directly from the part's actual manufacturer.

We looked at the activities and reported accomplishments of the breakout PCRs during fiscal years 1980 and 1981. Additionally, in our review, we examined the breakout efforts of the Odgen ALC's regular PCR for the same period because he was reporting substantial breakout accomplishments, even though breakout was not his primary function.

During this 1980 to 1981 period, SBA reported 294 breakout actions at the four ALCs and related savings of $7.3 million.

We tested 71 of the largest reported savings totaling $3.5 million. Although we found some problems with the methodology and rationale for estimating some of the savings, we concluded that SBA could reasonably claim credit for successfully breaking out 50 of the parts, involving reported savings of about $2.4 million. Forty-two of the 50 breakouts, totaling over $1.5 million, were awarded to small businesses, while 8 breakouts, totaling nearly $900,000, were awarded to large businesses. (Specific details for each ALC are included in the attachments.) Competition (two or more offerors) was introduced in 41 of these 50 procurements.

We did not agree with SBA's claimed savings on 21 of the cases. In most of these cases the ALC had either previously procured the part from the source identified by SBA or had already broken the part out for competition, but had failed to update its records.

SBA's reported savings, however, could very well understate actual breakout accomplishments. SBA officials have reported they are sometimes unable to calculate savings on subsequent purchases of items already broken out because of limited time and staff.

An example of how the participation of an SBA breakout PCR can result in a successful breakout follows:

The San Antonio ALC had been buying tube assemblies directly from the prime contractor since 1978. In August 1980, the Air Force issued a purchase request coded 3L (low dollar procurement--noncompetitive) and solicited a bid only from the prime contractor.

The SBA breakout PCR challenged the procurement method code. In response to this challenge, procurement officials at the San Antonio ALC recoded the procurement 3-H (incomplete data package). The breakout PCR again challenged the code. Procurement officials at the ALC then found the drawing in question, recoded the procurement for open competition, and issued a new purchase request.

The subsequent purchase of 661 units was competitively awarded to a small business at a price which was about $181 per unit lower than the price bid by the prime contractor and about $321 per unit less than the prime contractor's original sole-source bid in August 1980. The Air Force thus paid $212,498 less to buy the tube assemblies competitively, than if the prime contractor's original sole-source bid had been accepted.

Unfortunately, breakout progress has been, and will continue to be, slow unless the Air Force finds ways to effectively deal with a number of constraints which have hampered breakout efforts. These include:

--Incomplete information on who actually manufactures the parts for the prime contractor.

--Missing technical data with uncertainties as to whether data may be available elsewhere.

--Questions of whether the data is proprietary, and therefore legally unavailable to other suppliers.

--Reluctance on the part of ALC material management officials to accept the additional risk and inconvenience in procuring from a new source.

In spite of difficulties posed by these contraints, SBA's breakout efforts have resulted in large dollar savings relative to the program's costs. SBA's breakout efforts have also increased DOD's awareness of potential savings through breakout and have helped the Air Force identify new opportunities to obtain competition.

Within the next year, SBA would like to expand the breakout program by assigning breakout PCRs to a number of additional installations. We strongly support this action since effective use of these additional breakout PCRs should result in even greater savings to the Government.

Mr. Chairman, this completes my prepared statement. We would be pleased to respond to any questions you or other members of the committee have at this time.

ATTACHMENT I

ATTACHMENT I

SBA REPORTED SAVINGS FOR
Fiscal Years 1980 and 1981

	SBA		Reviewed by GAO		Breakouts validated by GAO		Breakouts not considered valid by GAO
	No. of Actions	Savings	No. of Actions	Savings	No. of Actions	Savings	No. of Actions
San Antonio ALC	110	$ 792,224	28	$ 656,670	15	$ 395,275	13
Oklahoma City ALC	82	1,198,520	15	981,001	8	685,262	7
Warner Robins ALC	16	940,628	16	940,628	16	940,628	0
Odgen ALC	86	4,388,541	12	924,479	11	405,703	1
Total	294	$7,319,913	71	$3,502,778	50	$2,426,868	21

ATTACHMENT II

ATTACHMENT II

Type of Business Awarded Breakout
Fiscal Years 1980 and 1981

	Small Business		Large Business	
	No. of Awards	Amount	No. of Awards	Amount
San Antonio ALC	14	$ 230,724	1	$164,551
Oklahoma City ALC	3	252,246	5	433,016
Warner Robins ALC	14	658,564	2	282,064
Odgen ALC	11	405,703	-	--
Total	42	$1,547,237	8	$879,631

Senator HAYAKAWA. Our next witnesses are Herman Director, chief economist/Federal contract specialist, National Small Business Association, and Lola Dickerman, cochairman, procurement committee, Smaller Business Association of New England.

Mr. Director, I shall welcome your testimony. It is already 11:35. I shall ask that you summarize your testimony to leave time for questions.

Please proceed.

STATEMENT OF HERMAN DIRECTOR, CHIEF ECONOMIST/FEDERAL CONTRACT SPECIALIST, NATIONAL SMALL BUSINESS ASSOCIATION

Mr. DIRECTOR. Thank you very much. I appreciate the opportunity to be here. In the interest of time, I shall submit the testimony for the record.

More attention should be paid to the problems of small procurement. Extension of the time allowed is sufficient, but, as we indicate, one of the most prolific occurrences is the response of no bid sets available to the people who request bid sets. It makes no difference whether you give 10 days, 45 days, or 1 year. If bid sets are not available, it makes no difference how much time you provide.

Another important constraint is that specifications are hard to get and limitations on distances, for example, are involved. You have to have an office within 25 miles of the site for procurement.

With current conditions of transportation and communication, it seems that that is an inhibiting restraint.

We also like to call attention to the fact that there are abuses to sole-source procurement procedures. As much as 85 percent of Government procurement is sole-source procurement.

I would like to emphasize that there should be a much greater enforcement of contracting out procedures required.

With regard to umbrella contracts, I would like to point out that they virtually make it impossible for small business to bid. For example, an umbrella contract which was issued in June of 1982, which lists various services for over $500,000, it is difficult for us to see how anybody but a large business could apply. It covers heating, ventilating, air-conditioning, maintenance operations, maintenance repair of buildings, family housing maintenance, grounds and surface, pest control, utility plant operation, motor vehicle operation, supply services, general mess operations, fire protection, guard services, custodial services, refuse collection, telephone service, and basic communication, and electronics. It is difficult to see that you need an umbrella of that size to effectively carry out the mission of our Government.

I think that these are continuing constraints which, as I indicate in my testimony on the last page, indicates we have been testifying on this subject in ordering changes in these constraints for the last 10 years, beginning in May of 1973. This goes through April 28 of 1982. We are now in September of 1982.

I am glad to see that there is continuing effort in this direction. I have been very active in the defense mobilization area, and I find that our efforts in that respect are falling very short of our needs. Whereas, at one time we had 4,000 small business people in the executive reserve to help under conditions of mobilization and conditions of civil disaster, it is down to less than 2,000 now. One of the biggest problems is making available the capabilities of small business that are absolutely necessary in these areas. If we do not do it by way of regular procurement and regular activities of Government, we will not be prepared.

In my experience I have worked during World War II, the Korean war, and the Southeast Asian war. There seems to be no end, so I urge the complete support of your proposed legislation, and it is interesting to note that SBA at least has come out in support of substantial portions of it while the administration and the Office of Federal Procurement Policy seem to think you can do all this by regulation.

There is a limit to what you can do by regulation. There are many, many contradictions in this. For example, on the simplifications of regulations in the Government generally on paperwork, Mr. Stockman's OMB office came out with a 22,000-word statement in the Federal Register on how to simplify regulations. I think that is a good indication of what we are up against.

Thank you very much, sir.

Senator HAYAKAWA. Thank you, Mr. Director.

[The prepared statement of Mr. Director follows:]

NATIONAL SMALL BUSINESS ASSOCIATION
"THE VOICE OF SMALL BUSINESS"

STATEMENT OF
HERMAN DIRECTOR
ON BEHALF OF THE
NATIONAL SMALL BUSINESS ASSOCIATION
BEFORE THE
SENATE SMALL BUSINESS COMMITTEE
HOLDING HEARINGS ON
S. 2446, SMALL BUSINESS PROCUREMENT REFORM
ACT OF 1982

SEPTEMBER 16, 1982

> **"It is the declared policy of the Congress that the Government should aid, counsel, assist, and protect, insofar as is possible, the interests of small business concerns in order to preserve free competitive enterprise..."**
>
> **(P.L. 85-536, as amended, Section 2(a), Small Business Act.)**

NSB Building • 1604 K Street, N.W., Washington, D.C. 20006 • Telephone (202) 296-7400

STATEMENT OF HERMAN DIRECTOR ON BEHALF OF THE NATIONAL SMALL BUSINESS ASSOCIATION BEFORE THE SENATE SMALL BUSINESS COMMITTEE HOLDING HEARINGS ON S. 2446, SMALL BUSINESS PROCUREMENT REFORM ACT OF 1982

SEPTEMBER 16, 1982

Mr. Chairman, members of the Committee. My name is Herman Director. I am appearing here today on behalf of the National Small Business Association (NSB), a multi-industry association representing approximately 50,000 small business firms nationwide. As chief of procurement matters for the National Small Business Association and as Federal contract specialist, I am involved in representation of NSB member firms in more than 1,000 standard industrial classification categories. This includes participation in and representation of small business before Federal agencies, including the Office of Federal Procurement Policy, and before various committees of Congress on Federal procurement matters with special emphasis on small business.

The National Small Business Association facilitates small business participation in government procurement through the Bidders Early Alert Message (BEAM) program.

When a company joins BEAM, it is asked to provide detailed information on the business: what goods and services are offered, what geographic areas can be served, what volume demands can be met, and so forth. This data is entered into the BEAM system.

Each day the government publishes the Commerce Business Daily (CBD), a list of everything it is seeking to buy from the private sector. This publication often includes as many as 800 requests for bids in a single day!

Requests for bids from the CBD are matched each morning to the details provided by BEAM members. The diversity and volume of opportunities to bid means that BEAM notices are mailed out every day.

But BEAM doesn't stop here. Each request for bids carries a deadline, and to make sure that BEAM members can meet the deadline, the BEAM staff often writes directly to the government agency that published the bid, and requests that bid documents be mailed to BEAM members.

And there's more. One BEAM member, a manufacturer of metal fence posts, received a contract to provide state survey stakes, because BEAM linked the government agency to a supplier with the correct capabilities. Before BEAM, though, the fence post maker had never considered selling survey stakes.

It has long been a standing policy of our government to rely on competitive private bids for goods and services it requires. Current expenditures for procurement are estimated to exceed $100 billion. The small business share has ranged between 20% to 25% for the past several years, representing no appreciable growth. The final figures for 1981, as reported by the Small Business Administration show that for fiscal year 1981, contract awards to small business totaled 19.6 billion or 21% as compared with 21.5 billion for fiscal year 1980, which represented 23.6% of total awards.

Detailed procurement records of 54 government agencies indicate that about half of the agencies report a small increase or no change in small business participation. There is obvious room for improvement in small business participation in government procurement, in view of the fact that small business accounts for 43% of the GNP and employs 58% of the nonagricultural working population. Small businesses are 95% of all private enterprises in the United States.

There has been an increasing tendency in government to compete with private business in providing additional "in-house" participation at the expense of commercial opportunities, even at higher costs to the taxpayer. This is counter to the goals of

P.L. 95-507, October 24, 1978, An Act to Amend the Small Business Act, and the Small Business Investment Act of 1958, which relates to government procurement for small business.

There are forces in government which oppose this policy and seek rather to expand the role of government in providing the services and products at the expense of small private business.

It's time to call a halt to the growing octopus of government, and it's time to live up to the promises of aid to the small business sector. Expand and enforce the implementation of A-76, which affirms the government's policy of reliance on the private sector to supply its needs.

OBSTACLES TO SMALL BUSINESS IN GOVERNMENT PROCUREMENT

A review and survey of small business experience with government practices indicates many obstacles to small business participation as follows:

OBSTACLE 1	Inadequate Time Allowed from the Time of Publication of Bid Notice to Bid Opening Date
OBSTACLE 2	Inadequate Time Allowed from Time of Publication of Bid Notice to Closing Date of Honoring Requests
OBSTACLE 3	Nonavailability of Bid Sets
OBSTACLE 4	Nonavailability of Specifications
OBSTACLE 5	Geographic Limits of Bidders Locations
OBSTACLE 6	Multiple Definitions of Size Standards
OBSTACLE 7	Rotation Policies on Bidders Lists
OBSTACLE 8	Sole Source Procurement

National Small Business in administering a procurement assistance program indicates that little, if any, progress has been achieved in overcoming these obstacles, although they have been called to the attention of Federal agencies and the Congress many times. As a matter of fact, the National Small Business records indicate that the eight obstacle conditions listed above have continued to multiply and get worse. The worsening conditions are mitigated only by the fine cooperation of the General Accounting Office (GAO), which is immediately responsive to protests which we file on behalf of our members. This recourse is, however, time consuming and costly. Our thanks, however, to the GAO.

There are, in addition, other obstacles to more competitive and small business participation in government procurement. These include:

1. Exclusion of nonappropriated funds from competitive bidding.
2. Noncompliance with Congressional intent. The Tennessee Valley Authority, for example, is not required to comply with procurement regulations except at a minimum. Virtually, all Federal Departments and Agencies frequently allow less than ten days for receipt of requests for bid sets and less than two weeks for "Bid Opening Date" from date when the first notice appears in the Commerce Business Daily.
3. The GSA is increasingly requesting payment of a charge for bid specifications.
4. Geographic limits on bid participation are narrowing in spite of communication and transportation improvements.
5. Small business set-asides are appearing less frequently.

6. Previous experience in actual performance of work for the government in the type of work specified is more often required. New participation is thus discouraged. This is especially prominent in Defense Department bids.
7. Extension of contracts for new work is more often reserved for current and previous contract performers, to the exclusion of new bidders who may be able to deliver the product at a lower price.
8. "Sole Source" bid invitations are increasing.
9. Performance by "In-House Resources" is increasing at the expense of competitive bidding.
10. As a matter of practice, solicitations often do not take into account performance, service, quality of results. They are awarded solely on the basis of lowest price.
11. Compliance with Labor Department Wage Determinations as required inhibit small business competition that depends on lower paid and often temporary help.

Not a single day goes by without obstructions, not only to small business participation in government procurement, but in the whole area of so-called "competitive bidding" in the public interest.

RECOMMENDATIONS:

1. Each agency or contracting office should have an active small business set-aside officer with specifically documented authority to monitor and establish set-asides for the small business community. As it is today, the small business set-aside often appears to be a

matter of happenstance or arbitrary decision -- just barely conforming to federal procurement policies. Further, a greater number of small business set-asides should be established for all types of business.

2. A minimum length of time, at least 45 days, as described in Section 4 of the proposed legislation, between the time a bid notice is published and the dates when both the requests for bid papers and the opening of the bids are announced should be specified by the Congress and adhered to by all Agencies of government. All too often, as is evidenced every day in the Commerce Business Daily, the time allowances are intolerably and impossibly short. Surely Contracting Officers, do not run purchasing on an hourly basis, nor is the receipt of bids and their openings so critical that reasonable lengths of time cannot be given.
3. There is no rational reason why there should be a lack of bid sets or specifications. Geographical limits should be defined to include all potential bidders.
4. Contracting officers should be trained to overcome the obstacles to small business participation in government procurement by instituting a special course of instruction in the Federal Procurement Training Institute of the Office of Federal Procurement Policy. The course should be designed to instruct procurement officers in the benefits and importance of advancing the position of small business in the procurement market, as well as how to conform with official procurement regulations.
5. Set up a recognition and award system for federal procurement officers who succeed in reducing costs and expanding new contractor participation in an agency.

6. Require bid notices for contracts directed toward big business capabilities to include an estimate of the dollar amounts and percentage of anticipated small business subcontracting.
7. Greater utilization of "multiple awards" in order to expand the base for small business participation, e.g., tires, food, and other broad-based items. This is particularly important and consistent with the government's Defense Preparedness Programm to assure alternate sources of essential supplies in the event of war or civil disaster. Dependence on sole source procurements can be extremely dangerous.
8. The Congress should establish a percentage goal for small business set-asides, as well as minimum levels of contract awards to small business, both for general procurement and for Research and Development.
9. Increased use of FOB Origin in bid specifications, so as to minimize the need to calculate transportation charges for multiple destination deliveries.
10. Letter of justification for selection of higher price bid as compared with lower offers.
11. Require preparation of contract awards reports on the basis of product or service procured rather than listing awards by procuring agencies; e.g., total awards for painting and small business amount; total awards for food, machine parts, hardware, etc., and the amount of awards to small business.
12. Participation by small business as prime contractors under umbrella-type contracts is virtually impossible. Inclusion of a broad range of services such as housing, maintenance, fire protection, telephone

> services, base communications and motor vehicle operation and utility plant operation make it virtually impossible for any but very large companies to bid directly as prime contractors. Reliance on subcontracting for small business participation is contrary to the small business goal of maintaining and fostering growth of new small businesses.

For decades now, Administrations of both parties have promised small business a "fair" share of Federal procurement. A firm minimum goal of 50% should be announced as a near term objective.

Federal Research and Development expenditure is even more concentrated against small business: less than 5% of the Federal total goes to small business. A five-fold increase in the R&D share for small business should be achieved within the next four-year period. Recent legislation requiring that 1.25% of all agency R&D budgets in excess of $100 million go to small business is a step in the right direction.

Unless Congress and the Administration take positive steps to increase the small business share of government procurement, they, by inaction, are furthering the growth of giantism and demise of small business in this country.

The Commerce Business Daily, in general, is a very difficult document to follow. It is designed in the format of the Federal Register rather than in the format of a usable business marketing working tool. It is poorly edited and printed. For example, "Live Animals" have been listed under "Ammunition" and "Medical Examination Tables" under "Construction and Mining Machinery". Other than through the NSB Procurement Assistance Program (BEAM) and SBA PASS, the Commerce Business Daily is practically the only source for small business to learn of sales opportunities to government.

The big companies do not rely on the Commerce Business Daily nor the U.S. Postal Service to maintain regular contact with contracting opportunities. Their practice is to maintain an office in Washington adjacent to the contracting office for daily "liaison" on procurement potentials and contract matters. As a matter of fact, the really big companies generally maintain three offices in the Washington area: one usually in the commercial center of town in the vicinity of the Executive Departments; one in Virginia near the Defense establishment and one in Maryland near NASA, ERDA, HHS and other agencies.

There is a need for a Market Planning Approach to solicitation of bids for federal procurement to increase competition and innovate more small business participation. The following are suggested keys to marketing.

1. Identify the product or service solicitation by four digit SIC.
2. List the application of the product.
3. Measure the size of the market quantitatively.
4. Locate the markets geographically, identifying large and small business separately.
5. Prepare county market data sheets for products in terms of numbers of companies available for solicitation.
6. Identify specific potential bidder companies by name and solicit these companies directly and add additional names as they become known.
7. Prepare and make available a short-term, six months and, where applicable, a long-term forecast of government requirements for products and services from the private sector, including both large and small businesses shown separately.
8. National Small Business is strongly in favor of establishing government procurement contracts arbitration panels as described in the proposed legislation.

National Small Business supports the passage of S. 2446, Small Business Procurement Reform Act of 1982, as it has supported similar legislative actions over the past ten years before Congressional Committees. A list of previous hearings in which we have testified in support of such legislation is enclosed. See ATTACHMENT I.

ATTACHMENT I

May 17, 1973	Senate Committee on Small Business hearings on Government Procurement
May 21, 1974	Senate Committee on Small Business hearings on The Problems of Small Business in Contracting with the Federal Government.
March 21, 1975	House Committee on Small Business on Problems of Small Business in Government Contracting.
June 29, 1976	House Committee on Small Business on Review of Government Procurement with Military and Civilian Agencies.
July 19, 1977	Senate Committee on Government Affairs on Federal Acquisition Act of 1977.
April 21, 1980	House Committee on Small Business on Federal Contracting Activities.
May 1, 1980	Senate Committee on Governmental Affairs on Year-End Contracting in the Federal Government.
June 16, 1981	House Committee on Small Business on Small Business Problems with Government Procurement.
April 28, 1982	House Small Business Subcommittee on SBA and SBIC Authority on A Bill to Improve Small Business Access to Federal Procurement Information.

Senator **HAYAKAWA**. Ms. Dickerman, we will be pleased to hear you.

STATEMENT OF LOLA DICKERMAN, COCHAIRMAN, PROCUREMENT COMMITTEE, SMALLER BUSINESS ASSOCIATION OF NEW ENGLAND

Ms. **DICKERMAN**. On behalf of the Smaller Business Association of New England, an association of 1,800 small businesses in New England, I have come to talk to you today in particular about section 6 of the bill which is before you.

I have been engaged as a lawyer representing small businesses in their disputes with the U.S. Government for something like more than 30 years. I would say that you have surely identified the problem, the single major problem, if I were asked to identify it—the costliness and length of the remedy process and the high cost of it, being such as to make it not a remedy to small businesses. That is the problem. Whether or not section 6 provides the best answer, I think is a real question.

I would suggest that rather than entertaining notions of new institutions or transferring responsibilities for this, that what we need to do is to simplify the processes and procedures. We have institutions intact and in place to do what we need to do.

Let me give you some simple examples. The process and procedure under the rules of the Armed Services Board of Contract Appeals today are exactly the rules which are followed by the Federal courts with all of the techniques of discovery, deposition taking, interrogatories, and the like. That is a very costly process. Very few small businesses could afford to be plaintiffs in the Federal courts under those procedures, and they cannot afford those procedures when they are adopted as they are now at the Armed Services Board and all the other boards.

Similarly, when a contractor finds himself in a dispute with the Government, he is frequently in the role of the defendant, that is, he has been found perhaps to be in default and being held for excess costs and the like.

The accelerated remedies that are in the disputes act deal with certain shortcut types of remedy for small dollar matters make a mistake in the equation. It suggests that small businesses will have small problems with the Government. That has not been my experience. The dollars involved in these kinds of disputes can run into very, very large numbers. I have seen them as much as $1 million, and not infrequently and very commonly as much as a half million dollars. Although we are talking about small businesses, these disputes can involve very large dollar amounts.

The Armed Services Board, has in place qualified persons to handle these matters, if those rules and regulations and the Contracts Dispute Act would permit small businesses to handle these matters, operating if they choose, to avoid the costly Federal rules of evidence and Federal rules of civil procedures which are presently in place. We would have the quicker, shorter process which is addressed in section 6 of this bill.

I would recommend to the committee essentially the following summary: You are on the right problem but this may not be the correct answer. I am speaking for myself and all the small businesses I have seen which have painfully had to give up their rights because they could not afford to pursue them. I would commend your attention to addressing this problem within the framework which exists today in the various agencies.

Thank you.

Senator HAYAKAWA. Are you saying, Ms. Dickerman, that you approve of the essential purpose of S. 2446?

Ms. DICKERMAN. Absolutely.

Senator HAYAKAWA. We are headed in the right direction?

Ms. DICKERMAN. In terms of your ultimate purpose, you are headed in the right direction. I think you have addressed two of the major problems in procurement—one, the getting of business through the breakout process; second, the resolution of disputes which you have also addressed. Those are the two critical areas.

Senator HAYAKAWA. But there are shortcomings in the bill as well?

Ms. DICKERMAN. Very serious shortcomings to the bill. I think that in section 6 the arbitration at SBA is not a good answer to the question. It is not necessarily the right way to go. I think it would not be used.

I have had experience with arbitration in Government contract disputes, and there are lots of good reasons it does not work well in those kinds of disputes.

I would like to see the small business disputes continue to be handled by the boards and agencies which handle them today, but under a different set of rules from the rules they use today.

Illustrative of this, the Contracts Dispute Act recently passed now requires certification in the absence of which the contractor loses rights.

Now, small businesses very often act for themselves in preparing their initial claims and would find themselves losing their rights in court without ever knowing they have done so.

Without going into detail, these are the kinds of things I refer to. I would like to see the way in which small business disputes are handled, changed, two tiered, if you will.

Senator HAYAKAWA. In what way?

Ms. DICKERMAN. I am suggesting they might be two tiered. That is to say, in a dispute between Boeing or Lockheed and the Government, I can understand the need or desire on the part of the contractor for the elaborate techniques used today, but I would like to see small businesses be able to operate for other kinds of rules, less costly and less lengthy.

Senator HAYAKAWA. Ms. Dickerman, I would be grateful if you would summarize your comments on S. 2446 in a formal letter to the committee so that we can study them and make an appropriate response and utilize your thoughts in the course of trying to improve this instrument.

Ms. DICKERMAN. Thank you very much. I would be glad to do that.[1]

Senator HAYAKAWA. Thank you.

Mr. Director, how would the abolishment of the Contracts Arbitration Panel benefit small business firms?

Mr. DIRECTOR. We find now, as Ms. Dickerman indicated, that most small businessmen give up because they have no resources. They do not know where to go or how. They are told to go to the nearest Department of Commerce office or to the contracting officer. We find there is very little effective communication.

While I am not as expert as Ms. Dickerman, I certainly would rely on her appraisal of this situation. However, there is need for some means, some more intimate means, of communication between the small businessmen and the agencies with whom they deal.

Senator HAYAKAWA. Are you advocating congressional action on your proposal for a marketing planning approach to bid solicitation?

Mr. DIRECTOR. I would like to see an indication by the Congress that they take a more direct approach to marketing procurement. In other words, when we go out in the private sector we go out to sell a product. We identify the product, we identify what it is used for, we identify the size of the market, identify its location, and then identify potential customers.

What I suggest is that similar procedures be used by the Government to increase the small business share of procurement in the same way, by identifying the product properly, putting it in the proper place.

For example, as I indicate, ladies shirts and blouses are listed under containers and packaging. We find hospital beds listed under a wide variety of engineering supplies. You have to be more careful there.

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[1] Information not available at time of going to press.

Actually what I am saying is that you have to identify things properly. If it is a table you are manufacturing, specifications for the table should be listed. You then decide who it is, find the names of small business companies. If it is done by small business companies, find the names of those companies and go and solicit participation from them in your procurement directly.

In the system we have now, the SBA has a system where the company can file a listing of products with the SBA and this then is sent to the contracting officer. He gives a list of names. There may be 100 or 200 names listed. He is required to call you only 1 time in 10.

I have had procurement officers from the procurement school or college come to me and ask, "What is your definition of competition?"

Their definition is three. If you can get three people to submit a bid, that is competition. This goes back to the contracting officer, who gets 100 requests, and he sends out bid sets. None other is available.

This is the sort of thing you have to get at in order to be intimately involved with procurement. The small businessman is there and he will compete.

Senator HAYAKAWA. Thank you.

Do you support the minimum time periods for advertising in the Commerce Business Daily contained in S. 1947?

Mr. DIRECTOR. Yes; I think that would be very useful in the elimination of time constraints. You can pick up the Commerce Business Daily almost every day and find it is impossible to bid.

I got a notice in the mail yesterday. The Commerce Business Daily was dated the 8th or 9th of the month. It said you had to make your request for the bids within 3 working days.

Well, we received it on the 11th or 12th. It was virtually impossible to get the bid in.

Here is a recent edition with regard to time constraints. This is on the 13th. It came in the mail yesterday, which was the 15th. The bid opening date is the 22d.

Here is another one. Bid opening date is the 21st. You know that is virtually impossible. There is not even enough time to get the bid papers, let alone bidding.

Senator HAYAKAWA. We discussed this matter months ago. Has it not been passed?

Ms. ELLIOTT. It has yet to be worked out in conference.

Senator HAYAKAWA. I understand it has been passed by the House, passed by the Senate, but it has not yet gone through conference. The things you complain of all have been taken care of except they are not finalized.

Mr. DIRECTOR. I can understand that. This happens in many instances. We are dealing with the Government and there is no way out. I can give you many, many personal instances of that.

Senator HAYAKAWA. Then we will try to help get it through during this Congress, which means within the next few days.

Thank you very much, Mr. Director and Ms. Dickerman.

We have Senators Specter and Levin's statements for insertion in the record. They were unable to get here. They will be inserted at this point in the record.

[The prepared statements of Senators Specter and Levin follow:]

STATEMENT OF HON. ARLEN SPECTER, A U.S. SENATOR FROM THE STATE OF PENNSYLVANIA

Mr. Chairman, I want to thank the chairman and the members of the Committee for holding this hearing on S. 2446, the Small Business Procurement Reform Act of 1982, introduced by myself, and my colleagues, Senators Weicker, Nunn, Baucus, Dixon, Glenn, Hayakawa, Packwood, and Riegle—many of whom are members of this distinguished committee and are here this morning.

I do not need to convince you gentlemen of the essential role America's 13 million small and independent businesses play in the Nation's economy, providing 55 percent of all private sector jobs and 50 percent of the gross national product. Small businesses are of special importance to the Northeast-Midwest region. A study done by Dr. David Birch of the Massachusetts Institute of Technology found that our region is almost entirely dependent on small firms for new job opportunities.

While small businesses are full and active partners in the economy as a whole, they have only limited access to the Nation's single, largest customer—the Federal Government's $110 billion annual procurement budget. Currently, only about 20 cents out of each dollar the Government spends to purchase goods and services goes to small firms, and that share is actually shrinking. Two years ago, the White House Conference on Small Business set forth a goal of increasing small businesses' participation in the Federal procurement process to 35 percent. Unfortunately, small business' share of Government contracts have declined since then from 22.2 percent in 1980 to 20.1 percent in 1981.

During the last year, I have sponsored a series of procurement conferences throughout Pennsylvania designed to facilitate small business involvement in the Government procurement process. At each session, I have had small businessmen and women recount frustrating experiences in attempting to do business with the Federal Government. Too frequently, it seems that the Government's procurement policies and practices discourage rather than encourage participation by small firms.

The Small Business Procurement Reform Act was designed to respond to these manifold concerns: lack of adequate time to prepare a bid; cumbersome paperwork; lack of information; restrictive bidding procedures; expensive and time-consuming litigation; and large systems contracts which preclude small business' participation.

Two major features of S. 2446 deserve the committee's close consideration. The first, referred to as "break out," would direct each federal agency to break its large systems procurement contracts, whenever feasible, into smaller components, thereby giving smaller firms a greater opportunity to submit bids.

Currently, many small businesses are automatically shut out of the procurement process by the sheer size of the large systems contracts offered by the Government—a practice which decreases competition and increases costs. In fact, a recent study by the Small Business Administration indicates that DOD alone wastes billions of dollars annually as a result of non-competitive bidding procedures on spare parts purchases. Although efforts are now underway within DOD to encourage the participation of smaller firms as prime contractors, these do not go far enough. Further steps are required—steps which will increase competition and diversity, cut government spending and strengthen the lower tiers of our ailing defense industrial base.

The breakout provision in this legislation is one such step. Initial results from a test "breakout" program conducted by the Small Business Administration's breakout efforts at Air Force Air Logistics Center (ALC's) are very promising. During fiscal 1980 and 1981, SBA offices at 4 air logistics centers reported savings of $7.3 million on 294 breakout actions. In a recent report to Congress, GAO found that "SBA's breakout efforts have resulted in large dollar savings in relation to the program's costs." The GAO report concluded, "opportunities exist . . . to realize even greater breakout accomplishments."

The Small Business Procurement Reform Act seeks to achieve these goals on a broader scale.

The second provision in S. 2446 I would like to focus on would authorize the Small Business Administration to establish arbitration panels to enable small businesses and government agencies to voluntarily submit to binding arbitration to resolve minor contractual disputes. The legislation does not specify the composition nor selection of these panels, but it has been suggested that the panels could consist of a rotating pool of attornies, accountants, and public representatives with expertise in the field.

I am aware that there are already a number of formal grievance procedures firms may pursue to seek resolution of contract disputes. A business may choose to: protest to the head of the particular procuring agency; protest to GAO; file a petition in federal district court; or, protest to the Board of Contract Appeals. All of these require time and money. With most contractual disputes involving amounts of less than $500,000, few small businesses can afford to become mired in lengthy litigation procedures. Rather than reinventing the wheel, arbitration panels provide an expedient and cost-effective medium for resolving contract grievances.

A third important provision of S. 2446, extending the bidding time on contracts to 45 days, has already been addressed by this committee in S. 1947, and passed both Houses of Congress. In addition, this bill would require agencies to inform small businesses when noncompetitive or restricted bids are issued, and require them to provide small firms with copies of appropriate regulations and other pertinent contract materials on a timely basis.

Although cost estimates have not yet been completed, preliminary experience with contract breakout indicates that implementation of S. 2446 may well result in a substantial net savings of tax-payer dollars.

In closing, I want to express my appreciation to the Committee and the Chairman for their time and support on this vital issue. The Small Business Procurement Reform Act provides a framework for a number of important reforms that will facilitate small business participation in the government procurement process, saving time and money for all parties involved. There are a number of areas that remain to be further defined in detail. I look forward to the comments and contributions of my esteemed colleagues on the Small Business Committee and to your earliest consideration of this measure.

STATEMENT OF HON. CARL LEVIN, A U.S. SENATOR FROM THE STATE OF MICHIGAN

Mr. Chairman, I want to commend you for holding this hearing and focusing the resources of the Committee and the attention of Congress on a procurement practice known as "breakout." Recently, through the reporting and Senate passage of S. 1947, this Committee has sought to ensure that small business are made aware of, and have sufficient opportunity, to respond to government procurement solicitations. Given this effort, it is only appropriate that we expand our review to a practice which could become another substantial source of federal procurement opportunities for small business.

The practice of breakout, which involves the separation of large system procurements into components of a size that will allow small business competition, is one that holds considerable potential for both small business and government. In light of this potential, it is surprising that breakout has previously received little, if any, attention by Congress. While a number of committees have held hearings on the procurement process, this is the first hearing to my knowledge in either the House or Senate to focus predominately on breakout. For these reasons, this hearing is an important beginning, and further demonstrates this Committee's commitment to improving procurement opportunities for small business.

It is a well know fact that small business are the most cost-efficient providers of goods and services. And where there is full competition for government contracts, and vigorous small business participation, the government has the greatest opportunity to achieve considerable savings over other forms of procurement. An expanded use of the practice of breakout would capitalize on this known fact to the benefit of small business, the government, and our nation's industrial base.

The benefits to the government of breakout and its potential for small business is highlighted in an August 2, 1982, report by the General Accounting Office (GAO). In that report, GAO examined a pilot program initiated by the Small Business Administration (SBA) to increase opportunities for small business in the procurement of spare parts by assigning "breakout" Procurement Center Representative (PCR) specialists at three Air Force air logistic centers (ALC's). A fourth ALC was also included in the review because of the substantial breakout activities by the "regular" PCR. GAO found that SBA offices at the four ALC's reported 294 breakout actions and associated savings of about $7.3 million during fiscal years 1980 and 1981.

Moreover, GAO found that of the $3.167 billion spent for spare parts by the four ALC's in fiscal year 1981, $619 million (19.3 percent) was awarded competitively, with the remaining $2.548 billion (80.7 percent) awarded on a sole-source basis. At a minimum, increased competition would likely increase procurement opportunities and awards to small business and save substantial sums for the government.

Senator Specter's bill, S. 2446, provides a basis for looking at ways to expand government use of breakout for small business. Toward that end it would establish a government-wide policy that procuring agencies make every effort practicable to subdivide large system procurements into smaller components to facilitate small business competition. Secondly, it would authorize the establishment of arbitration panels to resolve disputes over contracts between small business and the government. This is an approach that should be given further, serious consideration by Congress. In fact, I believe that arbitration and negotiation would work equally as well in developing new regulations. S. 1360, which I have sponsored, would provide for "regulatory negotiations." I ask that a copy of a September 7, 1982, Washington Post article on regulatory negotiations be included in the Committee record as an example of how this process might work.

I would strongly urge the Committee to schedule additional hearings on breakout in the near future. We need to ask both the civilian and military procuring agencies directly to what extent they are currently using, and whether they are capable of using, breakout to foster increased competition and procurement opportunities for small business. We need to explore in more detail the problems experienced by the agencies in using breakout, and how breakout efforts might be expanded.

As a basis for these additional hearings, I would suggest that the Committee focus on those constraints identified by GAO in its August 2, 1982, report in the area of spare parts breakout. It would also be appropriate to look at increasing the use of breakouts on new, large systems for competition by small business.

[From The Washington Post, Sept. 7, 1982]

THE FEDERAL REPORT—FLOATING A NEW RULE IN A HOT TUB MILIEU

(By Sandra Sugawara)

The process of writing a federal regulation is often fraught with delays and bloodied by the battles of adversaries, jousting over the issue at hand. A non-controversial rule change can take months, a controversial change years.

But now some people think there may be a better way: regulatory negotiation, or what one expert describes as the "hot tub" approach to writing federal rules.

Reduced to simple terms, says one report on the concept, it's as if everyone striped off their adversarial clothing and jumped in to trying to solve a problem with openness and honesty.

However, the author quickly noted, regulatory negotiations in reality would be far more complex. To start with, many parties would need considerable coaxing to take off their armor and dive in.

The report was prepared by Philip J. Harter for the Administrative Conference of the United States, a coordinating agency of fedeal officials and private attorneys that studies federal administrative and legal procedures.

Earlier this summer, the administrative conference voted to encourage federal agencies to use negotiations as an alternative to the traditional rule-making process. The concept also has sparked interest on Capitol Hill and in the Reagan administration.

In endorsing the concept, the conference noted that such negotiations hae been used successfully in establishing standards with extensive health, safety and economic effects for thousands of products and in settling lawsuits that have challenged regulations.

One reason federal agencies have been reluctant to use negotiations in developing proposed rules, the conference suggested, is that so many controls have been placed on an agency's behavior.

The conference cited the so-called ex parte rules, which are designed to restrict the ability of federal officials to meet privately with one side of a dispute; the Freedom of Information Act, which permits public access to the rule-making record, and the Sunshine Act, which opens many agency meetings to the public.

The conference urged Congress to enact legislation that would free agencies in certain cases from ex parte restrictions and public disclosure requirements. This would "provide substantial flexibility for agencies to adapt negotiation techniques to the circumstances . . . ," said the recommendation. The legislation, it said, should be viewed as an experiment that would expire after a certain time unless renewed.

However, one member of the conference, Consumer Product Safety Commission member R. David Pittle strongly objected. The newsletter Inside OMB quoted Pittle as saying, "While open meetings with outside parties may be inappropriate in agency activities" such as the settlement of a lawsuit, "it seems essential in the development of rules that would affect a whole industry and the consumers of that industry's product."

Nan Aron of the Alliance for Justice, a coalition of public interest groups that has been critical of the rule-making process under the Reagan administration, agreed with Pittle. "The reason the guidelines are there," she said, "is to protect the public from business and agencies getting together to promulgate rules directly affecting the public without the public's participation."

Aron noted that public interest lawyers generally would rather negotiate settlements than have to go to court. But she said, "The evidence of the Reagan administration so far is that they're excluding the public" by limiting public comment periods and meeting with industry groups. "I would query whether they would actually be fair-minded and set up a situation where all sides could be heard."

The conference recognized that not all regulations can be developed through negotiations and in some cases a consensus process would be even slower than the current rule-making procedures.

Ideally, the conference said the issue should be mature and ripe for a decision, and that a deadline should be set for issuing the rule. The issues selected also should not require any side to compromise its fundamental beliefs since it is unlikely that a consensus could be reached on such an issue. And all parties, it said, must believe they have something to gain from negotiations.

No party should dominate the negotiations, the conference added, not even the agency that will issue the rule. However, it said, the agency should not be forced to accept the outcome of the negotiations. Pittle was skeptical that these conditions would ever come together to allow negotiation of a significant rule. He said he could not "recall a single instance" during his nine years at the CPSC where all the conditions would have been met.

The conference's suggested procedures for regulatory negotiation are similar, in some ways, to the current rule-making process. Under the Administrative Procedure Act, which has been around since the New Deal, agencies are supposed to give notice that they are writing a new rule, seek public comments and analyze them before issuing a rule in final form. All steps along the way have minimum required time periods.

Under the conference's recommendation:

Congress would authorize agencies to appoint a "convenor," a neutral party to organize the negotiations. It could be an individual, an agency or a private organization. If an agency employee is chosen, that person should not be associated with the rule-making or enforcement staffs.

The convenor should decide whether negotiations are the proper way to proceed. The convenor should consider the factors outlined by the conference, as well as the effects a consensus decision could have on economic competition.

If the convenor decides that negotiations would be appropriate, it should notify the agency. If the agency concurs, the convenor must decide on the participants, the scope and the work schedule.

A notice should be printed in the Federal Register, and if additional groups ask to participate, a decision must be made by the convenor, in consultation with the agency.

After agreement is reached, the agency will write the proposed rule, guided (but not bound by) the negotiating committee. The proposal will be available for public comment, and the comments can be reviewed by the committee.

The final rule will be drawn up by the agency.

Senator **Hayakawa**. If there are no further questions, we may be writing to you.

That concludes the hearing.

[Whereupon, at 12 noon, the committee recessed, to reconvene at the call of the Chair.]

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